D.P.U/D.T.E. 96-24

Petition of Eastern Edison Company, pursuant to G.L. c. 164, §§ 76 and 94, and 220 C.M.R. §§ 1.00 et seq., for review of its electric industry restructuring proposal.

APPEARANCES: David Fazzone, P.C.
McDermott, Will & Emery
75 State Street
Boston, Massachusetts 02109-1807
FOR: EASTERN EDISON COMPANY
MONTAUP ELECTRIC COMPANY
Petitioners

L. Scott Harshbarger, Attorney General
By: Joseph W. Rogers
Assistant Attorney General
Regulated Industries Division
- and -
Edward G. Bohlen
Frederick Augenstern
Assistant Attorneys General
Environmental Division
200 Portland Street
Boston, MA 02114

Intervenor

Maribeth Ladd, Esq.
100 Cambridge Street, Suite 1500
Boston, Massachusetts 02202
FOR: DIVISION OF ENERGY RESOURCES
Intervenor

Stephen Klionsky, Esq.
260 Franklin Street, 21st Floor
Boston, MA 02110-3179
FOR: WESTERN MASSACHUSETTS ELECTRIC COMPANY
Intervenor

Paul Szymanski, Esq.
101 Ash Street
P.O. Box 126211
San Diego, California 92112-6211
FOR: ENOVA ENERGY INC.
Intervenor

Bernays T. Barclay, Esq.
Gregory K. Lawrence, Esq.
Wendy A. Barrett, Esq.
King & Spalding
120 West 45th Street
New York, New York 10036
FOR: IBC CORPORATION
Intervenor

Ned Hengerer, Esq.
Gordon J. Smith, Esq.
John & Hengerer
1200 17th Street, N.W.
Suite 600
Washington, D.C. 20036
FOR: ELECTRIC CLEARINGHOUSE, INC., EASTERN POWER DISTRIBUTION, INC., PANENERGY TRADING AND MARKETING SERVICES, L.L.C.
Intervenors

Peter W. Brown, Esq.
501 South Street
Concord, New Hampshire 03304
FOR: CRSS, INC.
Intervenor

Richard W. Benka, Esq.
Foley, Hoag & Eliot, L.L.P.
One Post Office Square
Boston, Massachusetts 02109
FOR: NEW ENERGY VENTURES, INC. AND XENERGY, INC.
Intervenors

Mark E. Bennett, Esq.
62 Summer Street
Boston, Massachusetts 02110-1008
FOR: CONSERVATION LAW FOUNDATION
Intervenor

Jerrold Oppenheim, Esq.
Nancy Brockway, Esq.
National Consumer Law Center
18 Tremont Street, Suite 400
Boston, Massachusetts 02108
FOR: ACTION, INC., MASSACHUSETTS ENERGY DIRECTORS ASSOCIATION, MASSACHUSETTS COMMUNITY ACTION ASSOCIATION, MASSACHUSETTS SENIOR ACTION COUNCIL, CAPE ORGANIZATION FOR RIGHTS OF THE DISABLED
Intervenors

John A. DeTore, Esq.
Robert D. Shapiro, Esq.
JoAnne Aylward Pierce, Esq.
Rubin and Rudman
50 Rowes Wharf
Boston, Massachusetts 02110
FOR: ENRON CAPITAL & TRADE RESOURCES
Intervenor

Richard J. Morrison, Esq.
John Cope-Flanagan, Esq.
COM/Energy Services Company
One Main Street, P.O. Box 9150
Cambridge, Massachusetts 02142-9150
-and-
Robert N. Werlin, Esq.
David S. Rosenzweig, Esq.
21 Custom House Street
Boston, Massachusetts 02110
FOR: CAMBRIDGE ELECTRIC LIGHT COMPANY, COMMONWEALTH ELECTRIC COMPANY, AND CANAL ELECTRIC LIGHT COMPANY
Intervenors

Ellen S. Roy
Senior Vice President
350 Lincoln Place
Hingham, Massachusetts 02043
FOR: INTERCONTINENTAL ENERGY CORPORATION
Intervenor

William C. Sheehan, President
P.O. Box 9116-265
Concord, Massachusetts 01742-9116
FOR: NORTHEAST ENERGY AND COMMERCE ASSOCIATION
Intervenor

Paul W. Gromer, Esq.
77 North Washington Street
Boston, Massachusetts 02114
FOR: NORTHEAST ENERGY EFFICIENCY COUNCIL
Intervenor

Neal B. Costello, Esq.
Executive Director
9 Park Street
Boston, Massachusetts 02108
FOR: COMPETITIVE POWER COALITION
Intervenor

Jon B. Hurst, President
18 Tremont Street, Suite 702
Boston, Massachusetts 02108
FOR: RETAILERS ASSOCIATION OF MASSACHUSETTS
Intervenor

Bruce F. Paul

Chairperson
42 Labor-in-Vain Road
Ipswich, Massachusetts 01938-2626
FOR: THE ENERGY CONSORTIUM
<u>Intervenor</u>

Joseph S. Fitzpatrick, Esq.
108 National Street
Milford, Massachusetts 01757
FOR: AMERICAN NATIONAL POWER
<u>Intervenor</u>

William Stowe, Esq.
Assistant General Counsel
800 Boylston Street
Boston, Massachusetts 02199
FOR: BOSTON EDISON COMPANY
<u>Intervenor</u>

Warren H. Pyle, Esq.
Bryan C. Decker, Esq.
Angoff, Goldman, Manning, Pyle & Wanger, P.C.
24 School Street
Boston, Massachusetts 02108
FOR: MASSACHUSETTS ALLIANCE OF UTILITY UNIONS
<u>Intervenor</u>

Peter B. McGlynn, Esq.
Bruce D. Levin, Esq.
Bernkopf, Goodman & Baseman, L.L.P.
125 Summer Street, 13th Floor
Boston, Massachusetts 02110
FOR: MERIDIAN MIDDLEBORO LIMITED PARTNERSHIP
<u>Limited Participant</u>

Douglas F. John, Esq.
John & Hengerer
1200 17th Street, N.W.
Suite 600
Washington, D.C. 20036
FOR: NEW YORK MERCANTILE EXCHANGE
<u>Limited Participant</u>

Alan R. Johnson
Manager, Electric Power Services
300 Friberg Parkway
Westborough, Massachusetts 01581
FOR: ENERGYEXPRESS, INC.
<u>Limited Participant</u>

Thomas E. Rodrigues

Business Manager, Local 1465
International Brotherhood of Electrical Workers
P.O. Box 1085
Fall River, MA 02720

FOR: INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS
<u>Limited Participant</u>

Herbert B. Levesque
P.O. Box 2885
Fall River, MA 02722

<u>Limited Participant</u>

Paul K. Connolly, Esq.
Patricia M. French, Esq.
LeBoeuf, Lamb, Greene, & MacRae
260 Franklin Street
Boston, MA 02110

FOR: UNITIL Fitchburg
<u>Limited Participant</u>

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I. INTRODUCTION

This Order addresses the Offer of Settlement ("Settlement") of electric industry restructuring issues for Eastern Edison Company ("EECo" or "Company") filed with the Department of Public Utilities, now known as the Department of Telecommunications and Energy ("Department"), by EECo and certain other parties. This Order presents the procedural history, a description of the new Electric Industry Restructuring Act, Chapter 164 of the Acts of 1997 ("Act")[1], a description of the Settlement, the Department's standard of review, and an issue by issue summary of the comments on the Act and the Settlement and our analysis and findings. The analysis and findings first address whether the Settlement is consistent or substantially complies with the Act (Section 193, Subsection 1A(a)) and second address whether the Settlement is consistent with Department precedent and in the public interest (the Department standard for reviewing all settlements).

II. PROCEDURAL HISTORY

In Electric Industry Restructuring, D.P.U. 95-30, at 47 (1995), the Department required each Massachusetts electric company to submit a restructuring proposal that includes, among other things, a plan (including any negotiated resolution) for moving from the current regulated industry structure to a competitive generation market and to increased customer choice. On February 16, 1996 EECo submitted its restructuring proposal, which the Department docketed as D.P.U. 96-24.[2] On May 16, 1997, EECo and Montaup Electric

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1 On November 25, 1997, Chapter 164 of the Acts of 1997, entitled An Act Relative to Restructuring the Electric Utility Industry in the Commonwealth, Regulating the Provision of Electricity and Other Services, and Promoting Enhanced Consumer Protection Therein, was signed by the Governor. All citations to the Act shall be to the Sections of Chapter 164 of the Acts of 1997.

2 On March 15, 1996, the Department opened a generic rulemaking to guide the development and evaluation of individual electric company restructuring plans. Electric Industry Restructuring, D.P.U. 96-100 (1996) ("D.P.U. 96-100"). On May 1, 1996, the Department issued proposed rules. D.P.U. 96-100, Explanatory Statement and Proposed Rules, May 1, 1996. On December 30, 1996, the Department, in the same docket, issued its plan for a restructured electric industry, including Model Rules and a Legislative Proposal. D.P.U. 96-100, Electric Restructuring Plan: Model Rules and Legislative Proposal, December 30, 1996.

(continued…)

Company ("Montaup") submitted a Settlement of the Company's restructuring proposal, along with a Joint Motion for Approval.[3]

Pursuant to notice duly issued, the Department received public comments,[4] and conducted two public hearings, in the Company's service territory, on June 24 and August 6, 1997. The Department conducted a procedural conference on June 24, 1997, at

(…continued)

In addition, the Department approved a settlement of the Massachusetts Electric Company restructuring plan, D.P.U. 96-25, on February 26, 1997 and an amendment of it on July 14, 1997, D.P.U. 96-25-A. The Department is also currently considering the restructuring plan of Boston Edison Company, D.P.U. 96-23.

3 The Settlement was signed by the Company, American National Power, the Attorney General, Competitive Power Coalition, Conservation Law Foundation, Intercontinental Energy Corporation, Massachusetts Division of Energy Resources, Northeast Energy and Commerce Association, Northeast Energy Efficiency Council, Retailers Association of Massachusetts, The Energy Consortium, and U.S. Generating Company.

4 The Department received comments on June 18, 1997 from Boston Edison Company; Enron Capital and Trade Resources; the Fall River Buying Group; [Electric Clearinghouse, Inc. Eastern Power Distribution, Inc., New York Mercantile Exchange, PanEnergy Trading and Market Services, L.L.C. ("Indicated Parties")]; [Action Inc., Massachusetts Energy Directors Association, Massachusetts Community Action Association, Massachusetts Senior Action Council, Cape Organization for Rights of the Disabled ("Low-Income Intervenors")]; Massachusetts Alliance of Utility Unions; New Energy Ventures (New England); and XENERGY, Inc.

which it granted petitions to intervene,[5] limited the scope of the proceeding,[6] and held four days of evidentiary hearings between July 9 and July 17, 1997.

In support of the Settlement, the Company presented the testimony of Michael J. Hirsh, vice-president of Eastern Utilities Associates ("EUA") Service Corporation, Dennis St. Pierre, vice-president of rates of EUA Service Corporation, Michael Laflamme, manager of treasury services of EUA Service Corporation, Carol White, manager of conservation and load

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5 The Department received a notice of intervention from the Attorney General pursuant to G.L. c. 12 § 11E and granted the petitions to intervene from American National Power; Boston Edison Company; Cambridge Electric Light Company, Canal Electric Company, Commonwealth Electric Company ("COM/Electric"); Competitive Power Coalition; Conservation Law Foundation; CRSS, Inc.; Enova Energy, Inc.; Enron Capital & Trade Resources; IBC Corporation; Indicated Parties; Intercontinental Energy Corporation; Low-Income Intervenors; Massachusetts Alliance of Utility Unions; the Massachusetts Division of Energy Resources; New Energy Ventures (New England); Northeast Energy and Commerce Association; Northeast Energy Efficiency Council; Retailers Association of Massachusetts; The Energy Consortium; Western Massachusetts Electric Company; and XENERGY, Inc. In addition, on July 9, 1997, the Department granted the petition to intervene of NorAm Energy Management, Inc.

The Department granted limited participant status to EnergyEXPRESS; Herbert Levesque; Meridian Middleboro Limited Partnership; New York Mercantile Exchange; and Thomas Rodrigues, Business Manager, Local 465, on behalf of the International Brotherhood of Electrical Workers. In addition, the Department granted the late-filed petition for limited participant status of UNITIL/Fitchburg.

6 The Department limited the scope of the proceeding to the following: Attachment 1 - the Company's unbundled tariffs that will be in effect until the retail access date; Attachment 2 - the Company's retail delivery tariffs with a standard offer option; Attachment 3 - Montaup's Stipulation and Wholesale Agreement with EECo; Attachment 5 - EECo's storm fund, unfunded deferred income taxes and FAS 106 amortization; Attachment 6 - the Company's performance standards under retail delivery rates; Attachment 7 - the Company's term sheet for bidding standard offer service; and Attachment 9 - Montaup's emission reductions from the Somerset and Canal 2 power plants. The Department excluded the following attachments from the scope of the proceeding: Attachment 4 - the Company's revised terms and conditions that reflect changes in the distribution company-customer relationship; Attachment 8 - the Company's terms, conditions, and settlement process with suppliers under retail delivery rates; and Attachment 10 - the Company's jurisdictional separation of transmission and distribution facilities pursuant to the Federal Energy Regulatory Commission's ("FERC's") Order 888. (Montaup filed the Company's jurisdictional separation of transmission and distribution facilities with FERC on June 1, 1997). In addition, the Department is currently considering the jurisdictional separation of transmission and distribution facilities of all the Massachusetts electric utilities in docket D.P.U. 97-93.

management services for EUA Service Corporation, and Peter D. Fuller, energy strategy adviser for EUA Service Corporation.

In opposition to the Settlement, XENERGY presented the testimony of James J. Walker, senior vice president. The evidentiary record consists of 114 exhibits and the responses to 27 record requests. Pursuant to the procedural schedule, the Department issued briefing questions on July 22, received initial briefs on August 1, and received reply briefs on August 8, 1997.[7]

On October 3, 1997, the Department issued a letter which indicated that several issues in the Settlement required clarification and that final action on the Settlement would be deferred until receipt of clarifying amendments. The Department sought amendments that would clarify that (1) the residual value credit would reflect periodic sales of specific assets within three months of completion of the sale of each asset; (2) Tariff No. 339 would clearly indicate that the retail access rates incorporate a maximum embedded access cost adjustment charge of 3.04 cents per kilowatthour ("KWH"), and that the actual level of the access charge is contingent upon the results of Montaup's divestiture activities; (3) residential and small general service (rate G-1) customers may elect to return to standard offer service within 120 days of first taking service from an alternative supplier; and (4) standard offer service customers may elect to continue taking standard offer service if they relocate within the

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[7] Initial briefs were submitted by the Attorney General, the Company, Enron Capital and Trade Resources, the Massachusetts Division of Energy Resources, Indicated Parties, Low-Income Intervenors, the Massachusetts Alliance of Utility Unions, New Energy Ventures (New England), and XENERGY.

Reply briefs were submitted by the Attorney General, the Company, Enron Capital and Trade Resources, the Massachusetts Division of Energy Resources, New Energy Ventures (New England), and XENERGY.

Company's service territory.[8] On October 10, 1997, the Company submitted revisions to the Settlement ("Revisions") intended to address the Department's concerns.[9]

On November 25, 1997, the Governor signed the Act into law. Among other things, the Act authorizes and directs the Department to require electric companies to accommodate retail access to generation services and choice of suppliers by retail customers and requires electric companies to file restructuring plans that comply with the statute. In addition, in recognition of the fact that certain restructuring settlements had already been filed with the Department, the Act provides that "an electric company that has filed a plan which substantially complies or is consistent with this chapter as determined by the department shall not be required to file a new plan, and the department shall allow such plans previously approved or pending before the department to be implemented." On December 5, 1997, the Department issued a notice seeking comments on whether the Settlement "substantially complies or is consistent with this chapter."[10]

III. DESCRIPTION OF THE ACT

In the Act, the Legislature found that ratepayers would be best served by moving from the existing regulatory framework, in which retail electricity service is provided principally by public utility corporations obligated to provide consumers in exclusive service territories with reliable electric service at regulated rates, to a framework within which competitive producers

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8 The Department provided an opportunity for amendment of the Settlement and comments on any amendments. October 3, 1997 Letter at 3. The Department did not receive any comments on the amendments.

9 The Revisions addressed each of the Department's concerns. The Department marks the October 3, 1997 letter from the Department and the October 10, 1997 letter and the attachments thereto from the Company as Exhibit DPU-69 and Exhibit EECo-2, respectively, and on its own motion, makes them exhibits in this proceeding.

10 On December 12, 1997, the Department received comments from the following: the Company, Conservation Law Foundation, Enron, LII, the Attorney General, and DOER. In addition, the Department received comments from XENERGY, Inc. on December 16, 1997.

will supply electric power and customers will gain the right to choose their electric power supplier. Section 1(c) of the Act. The Legislature found that the transition to a competitive generation market should be orderly, should be completed as expeditiously as possible, should protect electric system reliability, and should provide electric utility investors with a reasonable opportunity to recover prudently incurred costs associated with generation-related assets and obligations. Id. at § 1(s). Further, the Legislature found that the initial benefit of this transition to a competitive market shall be a rate reduction of at least 10 percent beginning on March 1, 1998, and 15 percent upon divestiture of generation assets and securitization. Id. at § 1(w).

The Act requires electric companies to file plans with the Department that implement a restructured electric generation market and offer retail access to customers by March 1, 1998. The plans must include the following: (1) an estimate and detailed accounting of total transition costs[11] eligible for recovery pursuant to G.L. c. 164, § 1G(b); (2) unbundled prices or rates for generation, distribution, transmission, and other services; (3) proposed charges for the recovery of transition costs; (4) proposed programs to provide universal service for all customers; (5) proposed programs and recovery mechanisms to promote energy conservation and demand-side management; (6) procedures for ensuring direct retail access to all electric generation suppliers; and (7) a discussion of the impact of the plan on the Company's employees and the communities served by the Company. Id. at § 1A(a). The Act mandates that the Department review the plans filed prior to enactment and judge their compliance with the law. The variety of the plans' principal features were known to the Legislature when, in passing the Act, it imposed on the Department this mandate to review the plans for consistency and substantial compliance.

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[11] Transition costs are also known as stranded costs and are discussed in Section IV.D, below.

Section 193 of the Act adds eight sections to G.L. chapter 164 ("G.L. c. 164"). The eight sections added to G.L. c. 164 deal with retail access and divestiture of generating plants (Subsection 1A), require overall rate decreases and service offerings (Subsection 1B), set rules for electric companies and their marketing affiliates (Subsection 1C), unbundle costs on customer bills (Subsection 1D), set standards for performance-based rates (Subsection 1E), delineate consumer protection and information rules for marketers and other electricity suppliers (Subsection 1F) , require mitigation and collection of identified transition costs (Subsection 1G), and allow for financial securitization to reduce transition costs (Subsection 1H).

Section 193, Subsection 1A of the Act enumerates the several requirements of each restructuring plan, as outlined above, but without detailing the particulars of each requirement. In addition, this subsection states that an electric company that divests its non-nuclear generation must separate ownership of its generation, transmission, and distribution facilities. Transmission and distribution facilities shall be transferred at net book value. Divestiture of non-nuclear generation may be accomplished by a competitive auction or assets may be transferred to an affiliate for a reasonable value.

Subsection 1B requires each distribution company to offer a standard service transition rate beginning March 1, 1998, with generation supplies procured by competitive bidding, for seven years to all its customers. The standard service transition rate, together with other charges, must provide an overall 10 percent rate reduction from August 1997 levels, before application of any residual value credit resulting from divestiture. After applying the residual value credit and/or implementing securitization, and by September 1, 1999, rates must be reduced by 15 percent from the original level. An inflation cap applies from March 1, 1999 through 2004. This subsection also provides that an electric company must offer default service, procured by competitive bidding with certain constraints, for customers whose supplier fails to deliver and to all customers after the standard service transition rate expires in 2005.

Subsection 1C provides that any marketing by an electric company shall be done by an affiliate separate from any generation, transmission, or distribution affiliate and states that a distribution company is prohibited from giving its affiliate any preference or advantage over non-affiliates.

Subsection 1D requires that a customer's electric bill show separate rates for distribution, transmission, generation, and transition (stranded cost) charges. Customers may elect a separate energy bill from their generation supplier.

Subsection 1E authorizes the Department to promulgate rules for performance-based rates for distribution companies, including standards, at a minimum, for customer satisfaction, service outages, telephone service, billing service, public safety, and benchmarks for employee staff levels and training programs, with limits on staff reductions. Companies must file performance reports annually and may be penalized up to 2 percent of their distribution and transmission revenues per year for failure to meet the standards.

Subsection 1F requires distribution companies to offer low-income discounts comparable to current ones, with expanded eligibility. The standard service transition rate must be available to low-income customers at any time.

Subsection 1G requires the Department to conduct a comprehensive audit[12] of each electric company to determine which generation-related costs may be recovered by a non-bypassable transition charge. Projected transition costs must be reconciled to actual costs at least every 18 months starting March 1, 2001, and power purchase contracts must be re-examined at least annually to determine above-market costs. A stranded cost charge may be

[12] Section 193, Subsection 1A provides that completion of a comprehensive audit by an outside accounting firm may be delayed until as late as March 1, 2000 for a company that filed a plan before enactment of the Act.

allowed for a company that commits itself to divestiture of non-nuclear generation, full mitigation of stranded costs (including renegotiation of above-market purchase power agreements ("PPAs"), and any other useful methods), a standard service transition rate for seven years, and overall rate reductions of at least 10 percent and later 15 percent. Eligible stranded generation costs may include the net book value of generating plant, nuclear decommissioning and post-shutdown costs, regulatory assets, above-market power purchase obligations, severance costs for most types of employees, and property taxes or payments in lieu of property taxes. The stranded cost charge is to be non-bypassable and collected by the distribution company, subject to a cap that does not change with inflation. The allowed rate of return on equity for as-yet unrecovered transition costs rises as the stranded cost charge falls and vice-versa, with a break-even point at two cents per KWH.

Subsections 1G and 1H also require an electric company to negotiate in good faith to reduce stranded costs from above-market PPAs[13] (except with municipal solid waste facilities ("MSW")), and does not allow recovery of stranded costs for the value of a contract change offered by a seller.[14] Electric companies may use securitization to finance buydowns and buyouts of power purchase contracts. An electric company may use securitization, if necessary after divestiture and renegotiating its PPAs, to further cut costs to attain the required rate reductions, as long as purchasers of divested generation have committed to continued employment for non-managerial plant personnel.

A number of other sections of the Act are pertinent. Section 37 of the Act requires a charge to fund cost-effective demand-side management ("DSM") programs for at least five

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[13] If a company assigns an above-market PPA to a buyer with adequate financial resources as part of a Department-approved divestiture plan, its obligation to renegotiate the PPA in good faith is met.

[14] For example, if a seller offered to reduce the price of a PPA from eight to six cents per KWH, which is still above market, the company could recover stranded costs only for the difference between six cents and the market price rather than eight cents and the market price.

years, beginning at 3.3 mills ($0.0033) per KWH in 1998, decreasing to 3.1 mills in 1999, 2.9 mills in 2000, 2.7 mills in 2001, and 2.5 mills in 2002. At least 20 percent of the residential portion, and at least 0.25 mills per KWH, must be used for low-income DSM and education programs. Section 50 of the Act authorizes DOER to oversee and coordinate ratepayer-funded DSM, with goals including equity among customer classes, low-income and weatherization programs, and support for lost opportunity programs, including statewide market transformation efforts. This section also requires the DOER to file an annual report with proposed DSM funding levels for the Department's approval to implement programs the Department finds to be cost-effective.

Section 37 of the Act requires a charge to fund renewable energy projects, with the fund to be administered by the Massachusetts Technology Park Corporation. This charge, to maximize economic and environmental benefits over time from renewable energy for Massachusetts, starts at 0.75 mills per KWH in 1998, followed by 1.00, 1.25, 1.00, and 0.75 mills per KWH for the years 1999 to 2002, and 0.50 mills per KWH thereafter.[15] Section 68 of the Act defines renewable energy eligible for funding from the ratepayer charge to include solar, wind, ocean-derived energy, landfill gas, advanced biomass, most fuel cells, MSW, hydro, and storage and conversion technologies connected to qualifying projects.

Section 71 of the Act provides that if restructuring causes a generation plant, especially a nuclear one, to be devalued for property tax purposes, the electric company must make payment in lieu of taxes according to a schedule over twelve years to offset any reduction of property taxes collected by a municipality.

Section 105 of the Act requires the Department of Environmental Protection to promulgate rules and regulations establishing uniform generation portfolio emission standards for fossil fuel-fired generating plants.

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15 Another part of Section 50 of the Act establishes a renewable energy portfolio standard to be administered by the DOER.

Section 315 of the Act requires a 10 percent or greater discount for agriculture or farming.

IV. DESCRIPTION OF SETTLEMENT

A. Introduction and Overview

The Settlement states that it would require a restructuring of the EUA system to further the Department's competitive market structure objectives and implement the restructuring plans of the Attorney General and the DOER (Exh. EECo-1, Vol. 1, at 5). The benefits of the Settlement include price reductions, access to competitive electricity suppliers for all customers, environmental protection, low-income protection, and support for a competitive regional market (id. at 7-37).

The Settlement states that it provides customers a 10 percent price reduction, guaranteed (subject to three possible adjustments) through 2004, which is accomplished by (1) reducing the access charge[16] compared to current rates and (2) providing a fixed stream of standard offer energy prices from 1998 through 2004 (id. at 7, 12). It provides for a base rate freeze, unbundled rates before the retail access date,[17] a standard offer energy price option after the retail access date, and an opportunity for all customers to choose any other electricity supplier (id. at 7, 24). The access charge is capped at 3.04 cents per KWH, is scheduled to decline after 2000, and will be further reduced by a residual value credit reflecting the proceeds from the divestiture, or sale, of Montaup's generating plants and PPAs (id. at 12). To further development of a competitive market, the Settlement requires Montaup to separate

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16 An access charge is used to recover those fixed generating costs that would be "stranded" by the transition to competition, because they could not be recovered in the energy price for electricity in the new market.

17 Section 193, Subsection 1A of the Act specifies that the retail access date will be no later than March 1, 1998. The Settlement provides for a retail access date which is the latter of January 1, 1998, or the date when retail access is made available to all customers of investor-owned utilities in Massachusetts (Exh. EECo-1, Vol. 1, at 6). Based on the Act, the Department finds that the retail access date provided for under the Settlement is March 1, 1998.

its transmission business from its generation business, requires Montaup to sell its generation business, and assures Montaup and EECo recovery of their fully mitigated stranded costs (id. at 5-6, 31-35).

The Settlement establishes a storm fund, performance standards for reliability and customer satisfaction, and a range for allowed return on equity (id. at 13-16). To protect low-income customers, the Settlement provides for safety net service, basic service, and low-income discounts for customers who might not otherwise receive, or might pay higher prices for, electricity (id. at 17, 22). To protect the environment, the Settlement provides for emission reductions from Montaup's two largest power plants, Somerset and Canal 2, increased funding for DSM, and funding for renewable energy resources (id. at 27-29; Vol. 2, at 245-246). The Settlement also contains several proposals which are not conditions for approval, including (1) defining which components of the Company's system are designated distribution and which are transmission, (2) proposed regional power reforms, and (3) terms and conditions of service for suppliers and customers (Exh. EECo-1, Vol. 1, at 23, 31-32).

B. Standard Offer

1. Introduction

"Standard offer" service (also known as "standard transition service") is the means by which EECo proposes to provide electricity supply to customers who do not choose competitive suppliers. Standard offer service would be provided on a transitional basis from the retail access date through December 31, 2004 only to those customers who had been taking service from the Company before January 1, 1998 (id. at 209). The retail access date is the later of January 1, 1998 or the date retail access is made available to all customers of investor-owned utilities in Massachusetts (id. at 24). After the retail access date, the total price, or retail delivery rate, that customers in EECo's service area would pay includes four components: (1) distribution charges, including rates based on performance standards for reliability and customer satisfaction, that would be effective until December 31, 2000; (2)

transmission charges that recover, on a reconciling basis, transmission service provided by Montaup, and any other charges billed to EECo for transmission service; (3) an access charge designed to recover costs associated with termination of the all-requirements service agreement between Montaup and the Company; and (4) an energy charge for electricity generated, which could be a charge for standard offer service provided through EECo or a charge arranged with a supplier of the customer's choice (id. at 11-12).

Standard offer service would be sought by EECo through competitive solicitation and would be available to all of the Company's retail customer classes (id. at 19-20). The Settlement sets out fixed standard offer retail prices for seven years, beginning at 2.8 cents per KWH on the retail access date and increasing to 5.1 cents per KWH in 2004 (id. at 209). These standard offer prices are subject to a fuel price index that takes effect after January 1, 2000. The Settlement sets out maximum wholesale standard offer prices, i.e., wholesale price caps during the standard offer period, which are the maximum amounts that will be paid to suppliers that bid to serve the Company's standard offer load (id., Vol. 2, at 204). For each of the first three years, 1998-2000, the wholesale price cap exceeds the standard offer price by 0.4 cents per KWH; thereafter, the maximum wholesale price paid to suppliers and the standard offer price paid by customers are the same. If the standard offer revenues collected by EECo do not recover EECo's payments to suppliers, then the Company may recover these shortfalls from standard offer customers, but only to the extent that the actual access charge falls below the unadjusted access charge set out in the Settlement (id., Vol. 1, at 21). If the actual access charge does not fall below the unadjusted access charge set out in the Settlement and if revenues are less than payments to suppliers, then EECo may defer these expenses with interest (id.). EECo may also defer underrecoveries in order to meet an inflation cap (id.).

2. Standard Offer Auction and Backstop Service

EECo intends to provide standard offer service by putting out a bid for standard offer power supply (id. at 19-20). Montaup is obligated to provide EECo with a standard offer wholesale supply at fixed prices increasing from 3.2 cents per KWH on the retail access date to 5.1 cents per KWH in 2004 (id., Vol. 2, at 204). This wholesale price cap is effective from January 1, 1998 to December 31, 2004 (id. at 204). For competitive suppliers to be eligible to provide supplies for standard offer service, their prices must be competitive with the wholesale prices that have been guaranteed by Montaup (id.). Montaup has an obligation to provide electricity supply for all standard offer customers in the event that competitive suppliers do not bid to provide electricity supplies for standard offer service, so called "backstop service" (id., Vol. 1, at 19). The Settlement provides that "[b]ackstop service would be provided by Montaup, its successor or assignee at the guaranteed wholesale price" (id.). An EECo affiliated power supply company may bid in the solicitation at prices less than the wholesale price cap (id. at 205). The winning bidders will be selected by June, 1998 (id. at 201-208).

3. Return to Standard Offer Service

The Settlement provides that, during the first year after the retail access date, except for residential and small general service (rate G-1) customers, customers who leave standard offer service for an alternative supplier may not return to standard offer service (id., Vol. 1, at 16). Under the Revisions to the Settlement, in the first year, residential and small general service customers may only return to standard offer service within 120 days of first taking service from an alternative supplier (id.).

C. 10 Percent Rate Reduction

The Settlement states that it provides for a price reduction of 10 percent or more for customers who choose the Company's standard offer pricing, which will be achieved through a two-step process (id. at 7).[18]

Initially, EECo's existing base rates will increase by approximately $1.5 million, or 0.5 percent over net operating revenues for the year ending June 30, 1997. First, base rates will incorporate two charges now billed separately: the Purchased Power Cost Adjustment ("PPCA") charge and the Energy Conservation Service ("ECS") charge (id. at 9, 43-44). Second, EECo will incorporate revised Conservation Cost Adjustment ("CCA") factors into base rates (id. at 9-10). The revised CCA factors provided under the Settlement represent an additional annual increase of approximately $1,526,500 over the CCA factors currently in effect (id. at 296-322). These increased ("Step One") rates will remain in effect until the retail access date (id. at 7).

The Settlement also provides that a DSM overrecovery balance of $4.18 million as of January 1, 1997, which would normally be returned to customers through lower rates, will be retained by the Company and used to mitigate the phased-in increase in the DSM and renewables budgets for 1998 through 2001 (id. at 26).

In Step Two, effective on the retail access date, the Settlement provides for a base rate reduction of 10 percent through an across-the-board reduction to EECo's Step One rates (id., at 7, 10, 250-286). Additionally, the Settlement provides for a base rate freeze through 2000 and possible further price reductions, depending on the success of mitigation efforts, future electricity commodity prices, a fuel price index, a floor on EECo's return on equity, and changes in accounting standards or tax laws (id., at 7-12, 20-23).

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18 Customers may choose to forego standard offer pricing because they expect even greater savings by doing so.

D. Stranded Costs

1. Introduction

The Department has defined stranded costs (also known as "transition costs") as those embedded costs of generation remaining after mitigation. D.P.U. 96-100, Model Rules: Section 11.03(3)(a). Embedded costs consist of the depreciated book value of owned generating plant, the minimum obligation under PPAs, generation-related regulatory assets, and nuclear decommissioning costs. Id. Mitigation includes sale of generating plant, sale of energy and capacity derived from PPAs and from owned generating plant, adjustments to PPAs that decrease the buyer's obligations, and writedown of assets. Id.

Pursuant to the Settlement, the present value of EECo's estimated stranded costs associated with the termination of the all-requirements service agreement with Montaup amounts to $601 million in the base case, i.e., when no mitigation occurs (Exhs. DPU-33; EECo-1, Vol. 2, at 55-56).[19]

2. Categories and Amounts of Stranded Costs

The Settlement's estimated stranded costs include both fixed and variable costs[20] (Exh. EECo-1, Vol. 2, at 55-56). In the base case, fixed costs represent two-thirds of the estimated stranded costs (id. at 58-60; Exh. DPU-33). The book value of Montaup's generating plant is $370 million, including $62 million for four fossil-fuel plants, $298 million for nuclear plants, and $9 million for other property (Exh. EECo-1, Vol. 2, at 58). The remaining fixed stranded costs include $24 million in regulatory assets and more than $10 million of nuclear costs independent of operation (id. at 59-60).

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19 EECo calculated an alternative estimate of $909 million for unmitigated stranded costs, using the FERC's formula set forth in its Order 888 (using a 15-year planning horizon from Department regulations), for an exit fee payable by EECo to Montaup if there were no Settlement (Exh. DPU-32).

20 Fixed costs are costs whose amount is known and certain, while variable costs are costs whose amount varies according to future conditions (id. at 38-53).

Estimated above-market costs[21] of PPAs under which Montaup buys power account for about 90 percent of the estimated variable stranded costs in the base case, or about 30 percent of total stranded costs (id. at 56). Nuclear decommissioning accounts for the rest of the estimated variable stranded costs, after allowing a credit for PPAs under which Montaup sells power (id.). For four types of stranded costs - PPA buyouts, payments in lieu of property taxes, employee severance and retraining, and damage claims - the dollar amounts are yet to be determined, but are presumed to be zero in the base case (id.).

Montaup, and in turn EECo, propose to collect their stranded costs in an access charge, over twelve years for fixed charges and over the lives of the obligations for the variable charges (id. at 54). The access charge is capped at 3.04 cents per KWH (id., Vol. 1, at 12).[22] In the base case, i.e., without mitigation, the access charge falls below 3.04 cents after three years, starting in 2001, gradually falling to 1.7 cents in 2009, then dropping to 0.86 cents in 2010, and falling slowly to zero in 2029 (id., Vol. 2, at 54).

3. Mitigation

The Settlement requires that Montaup divest, or sell, its generating plant (id., Vol. 1, at 33). Pursuant to the Settlement, Montaup filed a divestiture plan for approval by the Department and the FERC on July 1, 1997 (id. at 32). Montaup anticipates completing

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21 Above-market costs are the difference between the costs that the PPA requires the buyer to pay and the amount for which the buyer could resell the output acquired under the PPA. D.P.U. 96-100, Model Rules: Section 11.03(3)(a)(iii)1.

22 To maintain the access charge at the cap for the period 1998 through 2000, Montaup decelerates amortization of fixed stranded costs initially (Exh. EECo-1, Vol. 2, at 55). During 2001-2009, fixed stranded costs are amortized in equal amounts, resulting in a declining return of fixed assets and most of the decline in the overall access charge (id.). As discussed above, to the extent the access charge remains below the cap, EECo may charge standard offer customers for any loss it might incur from selling standard offer power below cost when wholesale market prices for electricity are high (id., Vol. 1, at 21).

the sale of its generating plant within six months of receiving all necessary regulatory approvals (id. at 33).[23]

The net proceeds of the divestiture will be used to reduce, or mitigate, the amount of stranded costs and in turn reduce the access charge, via a residual value credit, in equal amounts over the first twelve years, starting three months after asset sales (id. at 12; Vol. 2, at 8). If Montaup cannot sell its nuclear units, despite retaining decommissioning responsibilities, shareholders will assume 20 percent of the units' variable costs and keep 20 percent of the units' revenues (id., Vol. 2, at 18-19). The Company's ratepayers will assume the remaining 80 percent (id.).

The Settlement states that Montaup will try to sell, assign, or otherwise dispose of its PPA obligations to non-affiliates (id. at 19). The Settlement provides that PPA buyout expenses are entered into an annual reconciliation account which becomes active after 2000 (id. at 8-9, 19, 45). Until Montaup sells, assigns, or disposes of a PPA, the PPA's above-market costs will be flowed through to EECo and its customers via the access charge, as adjusted by the reconciliation account (id. at 45-50).

The Settlement provides that Montaup will receive an incentive for reducing the cumulative average access charge below 3.04 cents per KWH, calculated according to a table in the Settlement (id. at 46, 57).[24] The incentive is approximately three to four percent of the

23 If divestiture is not complete within three years, Montaup will report the reason for non-completion to the Department (Exh. EECo-1, Vol. 1, at 33). In return for Montaup's agreement to divest, the Settlement states that the Department, in a final determination, finds the access charge to be just and reasonable, entirely legal, in the public interest, and fully recoverable in distribution rates (id. at 36-7). Montaup may re-enter the generation business after divestiture is complete and sell at market rates, inside or outside of EECo's service area (id. at 37).

24 The marginal incentive is linear for cumulative access charges above 2.0 cents per KWH, linear but half as great for access charges of 2.0 cents to 1.0 cent, and is zero below 1.0 cent (Exh. EECo-1, Vol 2, at 57).

reduction in stranded costs, depending on the sale price of the assets (Exhs. DPU-34; DPU-35).

4. Other Aspects of Montaup's Wholesale Agreement with EECo

The Settlement proposes early termination of Montaup's wholesale agreement with EECo (Exh. EECo-1, Vol 1, at 7-8; Vol. 2, at 4). In addition to the access charge and divestiture, the Settlement includes a wholesale power rate freeze, a network transmission service agreement, and a mechanism for resolving access charge disputes between Montaup and any interested party (id., Vol. 2, at 4-13, 17-19). If Montaup divests any generating units before termination of its wholesale agreement with EECo, the Settlement allows recovery of reasonable replacement power costs, up to the amount customers would have paid absent divestiture, through Montaup's fuel clause (id. at 4-5).

E. Performance Standard Proposal

1. Introduction

The Settlement provides for a performance standard component based on service reliability and customer satisfaction as part of EECo's proposed retail delivery rates (id., Vol. 1, at 15, Vol. 2, at 198-199). Additionally, the Settlement provides that the Company submit for the Department's consideration a standard for the effective management of line losses by October 1, 1997 (id., Vol. 1, at 15). On October 1, 1997, EECo submitted its proposed line loss standard for the Department's consideration, including a set of criteria and penalties.

2. Service Reliability

The Settlement sets a base System Average Interruption Duration Index ("SAIDI")[25] of 81 minutes per year (id., Vol. 2, at 198). The 81 minutes per year is based on the average annual outage time for the years 1986 through 1996 of 67.3 minutes, plus the sample standard deviation of 13.2 minutes (id. at 200). The SAIDI excludes from consideration

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[25] The SAIDI is a standard measure in the electric utility industry which measures the total number of minutes the average customer is without service (Exh. DPU-18).

(1) interruptions lasting more than 24 consecutive hours affecting more than 10 percent of customers at the time of the outage; (2) interruptions of less than one minute; (3) interruptions resulting from the failure of other suppliers or transmission companies where restoration was beyond the control of the Company; and (4) extraordinary circumstances, such as earthquakes, blizzards, ice storms, and other major disasters (id. at 198; Tr. 1, at 49-58; Tr. 3, at 50-51).

The penalty schedule for service reliability performance, to be applied as a general credit, is set as follows:

Duration of Outage in Minutes	Penalty
up to 81 minutes	none
82 to 88 minutes	$62,500
89 to 95 minutes	$125,000
96 to 102 minutes	$187,000
103 or more minutes	$250,000

(Exh. EECo-1, Vol. 1, at 15; Vol. 2, at 200;).

3. Customer Satisfaction

The Settlement provides for a customer satisfaction standard, using the results of the EUA Customer Attitude Survey ("CAS") produced quarterly by Cambridge Reports Research International ("CRRI") (Exhs. EECo-1, Vol. 2, at 199; LII-11; Tr. 3, at 55-56). Using CRRI's top three categories of customer satisfaction under the CAS' seven-point scale, EECo determined that its average customer satisfaction rating for the period 1991 through 1996 was 80 percent (Exhs. EECo-1, Vol. 2, at 199; LII-11). Then the Company subtracted the sample standard deviation of 4.0 percent, to derive a net performance standard of 76 percent (Exh. EECo-1, Vol. 2, at 200).

The penalty schedule for customer satisfaction, to be applied as a general credit, is set as follows:

Percent of Responses in Top Three Categories (5, 6, and 7)	Penalty
less than 66 percent	\$250,000
67 to 69 percent	\$187,000
70 to 72 percent	\$125,000
73 to 75 percent	\$62,500
76 percent or more	none

(id.; Vol. 1, at 15).

F. Other Issues

1. Emission Reductions

The Settlement commits Montaup and its successors under divestiture to reduce emission rates of nitrogen oxides ("NO_x") and sulfur dioxide ("SO_2") from Somerset and Canal 2, starting in 2000 (Exh. EECo-1, Vol. 1, at 25; Vol. 2, at 240-242).[26] Targets may be met using any combination of controls, fuel switching, allowances, retirements, or other means (id., Vol. 2, at 242). The targets are 0.3 pounds per million British thermal units ("MMBtu") for SO_2 and 0.15 pounds per MMBtu for NO_x for May through September, which is the ozone season (id. at 240-242).[27] These targets constitute a 75 percent reduction from Somerset's 1994 NOx and $S0_2$ emission rates (id. at 245-246).[28]

2. Demand-Side Management

The Settlement requires EECo to submit to the Department budgets for DSM, including market transformation, for 1998, 1999, and 2000 based on a charge of 3.0 mills per KWH,

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[26] The NO_x standard does not apply to Canal 2 until 2010 (id. at 242).

[27] The NO_x standard is 0.21 pounds per MMBtu for the rest of the year (id.).

[28] The NO_x reduction is 61 percent from the reduced 1997 emission rates (id. at 245-246). The Settlement does not show past or present emission rates for Canal 2, a unit in which Montaup holds an ownership share.

followed by a charge of 2.75 mills in 2001 (id. at 26-27).[29] At least 15 percent of the DSM budget must be spent on residential programs, with at least 15 percent of that for low-income programs, including specific amounts for weatherization and fuel assistance (id.). The DSM budget includes money for the Energy Conservation Service program, EECo's DSM programs, lost base revenues, pilot projects, distributed generation and targeted DSM, and up to $0.4 million in any year and $0.8 million total for sophisticated DSM metering and control (id. at 27). The Settlement allows EECo to begin recovery of DSM expenses at the budgeted rate, through increased conservation charges to all customers, upon approval of the Settlement (id. at 9-10).

3. Renewables

The Settlement requires EECo to submit to the Department for its approval annual budgets that increase from $0.65 million to $3.25 million for the commercialization of renewable energy technologies,[30] based on collection from ratepayers of 0.025, 0.055, 0.085, and 0.125 cents per KWH for the years 1998 through 2001, respectively (id. at 27). The Settlement sets a goal, without a penalty, of four percent of all Massachusetts electricity sales from these technologies by 2007, provides for net metering for renewable generators under 30 kilowatts ("KW"), and provides for input by signatories to the Settlement into Department decisions after 2001 concerning continued funding for renewables and DSM (id. at 28-30).

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[29] EECo's current $4.18 million DSM overrecovery balance will be used to mitigate the phased-in increase in the DSM/renewables budget and support collaborative market transformation research (id.).

[30] The Settlement categorizes solar energy; wind energy; ocean thermal, wave, or tidal energy; landfill gas; and low emission advanced biomass power conversion technologies as forms of renewable energy eligible for funding (Exh. EECo-1, Vol. 1, at 28-29). The Settlement includes fuel cells as a technology eligible for funding (id. at 29).

4. <u>Low-Income, Default, and Basic Service</u>

The Settlement provides that EECo's 35 percent low-income discount, rate R-2, is retained for electricity prices [less fuel costs], by applying a larger discount to distribution costs (including the access charge), and no discount to the standard offer or transmission charge (<u>id.</u> at 30, 48, 51, 213, 216). The discount is available to customers who currently receive benefits from any of several low-income programs (<u>id.</u> at 50). Suppliers can bill EECo directly for energy delivered to low-income customers, leaving EECo with the credit risk of non-payment (<u>id.</u>).

The Settlement provides for safety net service for customers unable to obtain or retain electric service from competitive power suppliers, as well as basic (default) service for customers who may be temporarily without a contractual relationship with a power supplier (<u>id.</u> at 22). EECo will provide default service as necessary, procured from the short-term wholesale market (<u>id.</u> at 22).

5. <u>Storm Fund</u>

The Settlement permits EECo to create a storm reserve fund to pay the incremental costs associated with major storms, defined as storms resulting in incremental costs exceeding $250,000 (<u>id.</u>, Vol. 2, at 192; DPU-7; DPU-8). Under the Settlement, the Company will prefund the storm reserve by transferring a sum of up to $2 million from the Montaup 1996 Purchased Capacity Adjustment Clause ("PCAC") refund to the Company (Exh. EECo-1, Vol. 1, at 13). Effective with the retail access date, EECo's retail rates will be deemed to provide for a $1.3 million annual accrual to the storm reserve fund through monthly contributions to the reserve, until otherwise modified by the Department (<u>id.</u>).

6. FAS 106 and FAS 109 Obligations

As of December 31, 1996, the Company had a net federal and state deferred income tax deficit calculated in accordance with Financial Accounting Standards ("FAS") 109 of $2,643,480, and costs for deferred post-retirement benefits calculated in accordance with FAS 106 of $1,158,501 (id., Vol. 2, at 195-196). Under the terms of the Settlement, EECo's retail delivery rates incorporate a three-year amortization of all remaining unfunded FAS 109 obligations arising from state and federal deferred income taxes, commencing with the effective date of the retail delivery rates (id., Vol. 1, at 15; Vol. 2, at 195). In addition, EECo's retail delivery rates have been developed under the assumption that the Company's FAS 106 obligations related to its retail operations will be amortized over the period between January 1, 1997 and December 31, 2000 (id., Vol. 1, at 14).

7. Employee Issues

The Settlement provides that all reasonable costs and expenses incurred by Montaup or its affiliates associated with the implementation of retail access, divestiture, or termination of Montaup's tariff, such as early retirement, severance, retraining, and other related expenses, shall be incorporated in the access charge (id., Vol. 2, at 51-52).

8. Annual Price Adjustments

The Settlement provides EECo with the opportunity to adjust its retail delivery rates for the effect of any changes in tax rates or laws, or any externally-imposed accounting changes, which affect the Company's costs by more than $125,000 per year (id., Vol. 1, at 12-13; DPU-57). The Company states that there are no current tax or accounting proposals under published review by the accounting industry which would necessarily trigger this provision (Exh. DPU-57).

Moreover, the Settlement allows EECo to adjust its rates each April so that its average return on equity ("ROE") falls between 6.0 percent and 11.0 percent (Exh. EECo-1, Vol. 1, at 11). If, in a given year, the Company's ROE falls below 6.0 percent, using the data from

EECo's annual report to the Securities and Exchange Commission, but eliminating its investment in Montaup, the Company is permitted to increase its rates by a uniform cents-per-KWH surcharge sufficient to provide an ROE of 6.0 percent (id. at 11-12; DPU-12). If the Company's calculated ROE for a particular year exceeds 11.0 percent, but is less than 12.5 percent, EECo shall reduce its rates by a uniform cents-per-KWH credit to refund 50 percent of the excess earnings (Exh. EECo-1, Vol. 1, at 11-12). Any earnings over 12.5 percent shall be returned to customers in full through the refund mechanism (id.; Exh. DPU-13).

9. Proposed Unbundled and Retail Access Tariffs

As part of the Settlement, EECo has submitted two sets of tariffs. The first set, M.D.P.U. Nos. 322 through 337, consists of tariffs that have been redistributed into distribution/access, transmission, and generation components ("unbundled tariffs"), which would remain in effect from the date of this Order until the retail access date, i.e., March 1, 1998 (Exh. EECo-1, Vol. 1, at 41-85).[31] The unbundled tariffs reflect the fact that the Company's current PPCA and PPCA reconciliation adjustment, revised CCA charges, and the current ECS charge are rolled into base rates (id. at 9-10). The unbundled tariffs also provide that EECo shall close its Large Primary Voltage Auxiliary General Service Rate A-6, Economic Development Rate Rider ED, and Interruptible Load Rider ILR to new customers (id. at 10).

The second set, M.D.P.U. Nos. 338 through 356, consists of the Company's retail delivery tariffs with the standard offer option that will take effect as of the retail access date, i.e., March 1, 1998 (id. at 206-248). Among the Company's proposed retail delivery tariffs are two new schedules: a Transmission Cost Adjustment Clause ("TCAC") and an Access Cost Adjustment Clause ("ACAC"). The TCAC, M.D.P.U. No. 338, is intended to recover,

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[31] Because the tariffs filed as part of the Settlement are designated as attachments to the Settlement and carry a proposed effective date of July 1, 1997, EECo would have to submit a compliance filing even if the Settlement were approved without modification.

on a fully-reconciling rate class-specific basis, the transmission charges billed to EECo by Montaup, as well as any charges billed to EECo by or for the benefit of a regional transmission group, independent system operator, other transmission provider, or any regional entity that may be established to provide transmission or reliability operation services under FERC jurisdiction (id. at 203-204). The ACAC, M.D.P.U. No. 339, is intended to recover, on a fully reconciling basis, the contract termination charges billed to EECo by Montaup under the wholesale rate settlement (id. at 204).

The access charge under the ACAC has been fixed initially at 3.04 cents per KWH, which will remain in effect through December 31, 2000 (id.). The ACAC in the original Settlement reads: "[t]he access cost adjustment factor shall be [3.04 cents]/KWH through 2000. Thereafter, the factor shall be adjusted each time that the termination charge that MEC [Montaup] bills to the Company changes" (id. at 208). Under the Revisions to the Settlement, the ACAC has been rewritten to note that the access charge of 3.04 cents per KWH was embedded in the retail access rates, to clarify other provisions, and to specify that the residual value credit would be that allowed by the FERC, upon the divestiture of Montaup's non-nuclear generating units as it occurs (Exh. EECo-2).

V. STANDARD OF REVIEW

The Department has broad authority to regulate the ownership and operation of electric utilities in the Commonwealth. See, e.g., G.L. c. 25, §§ 5, 9, 18, 19, and 20; c. 111, §§ 5K and 142N; and c. 164, §§ 1 through 33, 69G through 69R, 71 through 75, and 76 et seq. This authority was most recently revised and augmented by the Act. The primary goal of the Act is to establish a new electric utility "framework under which competitive producers will supply electric power and customers will gain the right to choose their electric power supplier" in order to "promote reduced electricity rates." Section 1 of the Act.

Among other things, the Act authorizes and directs the Department to "require electric companies organized pursuant to the provisions of [G.L. c. 164] to accommodate retail access to generation services and choice of suppliers by retail customers, unless otherwise provided by this chapter. Such companies shall file plans that include, but shall not be limited to, the provisions set forth in this section." Section 193, Subsection 1A(a) of the Act. Pursuant to its statutory authority, the Department will review a Company's restructuring plan for compliance with applicable provisions of the Act.

The Act sets forth explicit directions for the Department's review of restructuring plans. Plans must contain two key features. They must provide, by March 1, 1998, a rate reduction of 10 percent for customers choosing the standard service transition rate from the average of undiscounted rates for the sale of electricity in effect during August 1997, or such other date as the Department may determine. Id. Each plan must be designed to implement a restructured electric generation market by March 1, 1998, and each electric company must offer retail access to all customers as of that date. Id.

Plans must also include the following important attributes:

(1) an estimate and detailed accounting of total transition costs eligible for recovery pursuant to G.L. c. 164, § 1G(b);

(2) a description of the company's strategies to mitigate transition costs;

(3) unbundled prices or rates for generation, distribution, transmission, and other services;

(4) proposed charges for the recovery of transition costs;

(5) proposed programs to provide universal service for all customers;

(6) proposed programs and recovery mechanisms to promote energy conservation and demand-side management;

(7) procedures for ensuring direct retail access to all electric generation suppliers; and

(8) discussions of the impact of the plan on the Company's employees and the communities served by the Company.

Id.

The Act directs the Department to allow the implementation of plans filed before the enactment date: "An electric company that has filed a plan which substantially complies or is consistent with this chapter as determined by the department shall not be required to file a new plan, and the department shall allow such plans previously approved or pending before the department to be implemented." Id. The Department will take these statutory directives into account in determining whether a plan should be approved for implementation.

In determining whether a plan substantially complies or is consistent with Chapter 164, the Department will consider as a whole the stated purposes and goals of the Act as enumerated and declared by the Legislature. See, e.g., Sterilite Corp. v. Continental Casualty Co., 397 Mass. 837, 839, n.3 (1986). The plain language of the statute gives the Department broad discretion to implement those stated purposes and goals and a mandate to do so in a timely manner, consistent with the Legislature's declaration of the Act as an emergency law, necessary for the immediate preservation of the public convenience:

> The deferred operation of this act would tend to defeat its purpose, which is to establish forthwith a comprehensive framework for the restructuring of the electric utility industry, to establish consumer electricity rate savings by March 1, 1998, and to make other changes in law, necessary or appropriate to effectuate important public purposes.

Id., Preamble.

The statute directs the Department to approve any plan that was filed before enactment, provided it "substantially complies or is consistent with this chapter." Id., § 1A(a). An action "substantially complies" if it achieves "compliance with the essential requirements" of the statute. Black's Law Dictionary, Sixth Edition (1991). An action that is compatible with and not contradictory of a statute is "consistent" with the statute. Id. The use of these terms in the disjunctive compels the conclusion that the Legislature has given the Department considerable discretion to effect the important public purposes of the Act. In addition, the Legislature has mandated it to do so swiftly (i.e., before March 1, 1998).

In setting the standard of review, the Legislature recognized that one settlement had already been approved and other settlements were pending before the Department.[32] Therefore, in order to retain the value of extensive negotiated settlements among a divergent group of signatories, the Legislature did not require strict compliance with every particular of the Act; instead it stated that these settlements must be evaluated based upon consistency with or substantial compliance with the Act. To be approved as substantially compliant, a settlement need not comply strictly point by point with the Act, but must, on the whole, achieve actual compliance with respect to the essential requirements of the statute. In short, the Legislature was aware of two points when it passed the Act: (1) The three settlements were negotiated by essentially the same set of negotiators and achieved remarkable congruence on fundamental points that were later featured in the Act; yet (2) there were numerous company-specific divergences in details among the settlements and between the settlements and the Act.

Against this background, the Legislature directed the Department to achieve retail access within three months and granted the Department broad authority to assess the settlements for consistency or substantial compliance with the terms of the Act. Because the phrase "substantially complies or is consistent with" is imprecise, the Department supplements its understanding of the words in the statute (customarily, "the principal source of insight into legislative purpose," Bronstein v. Prudential Insurance Co., 390 Mass. 701, 704 (1984)), with a consideration of "the statute's purpose and history." Sterilite, 397 Mass. at 839. A more limiting interpretation would defeat the Act's purposes and fail to give "a fair consideration of the conditions attending its passage." Fickett v. Boston Fireman's Relief Fund, 220 Mass.

32 At the time of enactment, the Department had approved the MECo settlement. In addition, EECo and Boston Edison Company had filed offers of settlement, which were under Department review. Further, collectively, Commonwealth Electric Company, Cambridge Electric Light Company, and Canal Electric Company filed their restructuring plan on November 19, 1997, before engrossment of the Act.

319, 320 (1915). The Legislature intended that the Department move with dispatch to review the settlements already filed by declaring the Act to be an emergency law. The Legislature established March 1, 1998 as the retail access date and clearly intended that the Department complete its review of settlements expeditiously. Accordingly, it granted latitude to review for substantial, rather than precise, compliance with the Act. The Department further notes that the Act refined the scope of the Department's already broad authority with respect to restructuring and the recovery of stranded costs. That authority was vested in the Department by the Legislature before the passage of the Act. See, e.g., Massachusetts Institute of Technology v. Department of Public Utilities, 425 Mass. 856, 867 (1997) (recognizing authority of Department to allow recovery of stranded costs as implicit in its broad authority). Therefore, we must consider the settlement and make a determination whether it satisfies, on the whole, the stated goals and main features of the Act.

In this case, the Company has filed its restructuring plan in the form of a settlement. The features of this and other electric restructuring settlements were known to the Legislature in its deliberations leading to the Act. In assessing the reasonableness of an offer of settlement, the Department reviews the entire record as presented in a company's filing and other record evidence to ensure that the settlement is consistent with applicable law, including relevant provisions of the Act, Department precedent, and the public interest. Berkshire Gas Company, D.P.U. 96-92, at 8 (1996); Boston Gas Company, D.P.U. 96-50, at 7 (Phase I) (1996); Massachusetts Electric Company, D.P.U. 96-59, at 7 (1996). A settlement among the parties does not relieve the Department of its statutory obligation to conclude its investigation with a finding that a just and reasonable outcome will result. Essex County Gas Company, D.P.U. 96-70, at 5-6 (1996); Fall River Gas Company, D.P.U. 96-60, at 5 (1996).

In assessing whether an electric company's proposed settlement of restructuring issues is consistent with applicable law and Department precedent, the Department will consider whether the settlement is consistent with the overall goal and principles for restructuring that were established in the Act and the Department's two major restructuring orders, Electric Industry Restructuring, D.P.U. 95-30 (1995), and Electric Restructuring Plan: Model Rules and Legislative Proposal, D.P.U. 96-100 (1996), to the extent the terms of those orders are not superseded by the Act. A plan, filed as a settlement, that strikes an appropriate balance among the various competing interests in electric restructuring, and that achieves an orderly transition, all consistent with applicable law, Department precedent, and the public interest, should be approved for implementation.

VI. ISSUES

A. Introduction

The following are all issues in the Settlement that have been commented upon by one or more of the parties or are deemed important by the Department. We make findings on each issue separately and then, in our conclusion, determine whether the (1) the Settlement substantially complies or is consistent with the Act and therefore shall be implemented, and (2) whether, as a whole, the Settlement is just and reasonable and in the public interest. We begin by analyzing the Settlement to see if it qualifies as a restructuring plan or if the Company needs to refile. We then analyze the Company's standard offer proposal and three models which have been proposed to alter it: Enron's model to eliminate the backstop obligation; XENERGY's model to include a comparability credit; and an option which would eliminate the standard offer deferral and reduce the access charge. Then we analyze the standard offer auction; the 10 percent rate cut; stranded costs; the performance standard proposal; emission reductions; demand-side management ("DSM"); renewables; low-income, safety net and basic service; the storm fund; employee issues; and the proposed unbundled and retail access tariffs.

B. The Settlement as a Restructuring Plan

1. The Act

Section 193, Subsection 1A of the Act requires that each restructuring plan must provide for retail access, i.e., choice of suppliers, for all customers by March 1, 1998 and a minimum 10 percent rate reduction for customers choosing the standard service transition rate. A restructuring plan must include an accounting of transition costs, plans to mitigate and collect transition costs, unbundled rates, direct access to retail suppliers, universal service, DSM programs, and a discussion of the plan's impact on employees and communities. An electric company that divests its non-nuclear generation must separate ownership of its generation, transmission, and distribution facilities, transferring transmission and distribution facilities at net book value. Divestiture of non-nuclear generation may be accomplished by a competitive auction, or assets may be transferred to an affiliate for a reasonable value.

2. The Settlement

The Settlement provides for retail access starting on the later of January 1, 1998 or the date retail access is generally available in Massachusetts (Exh. EECo-1, Vol. 2, at 6). The Settlement states that it guarantees a 10 percent rate reduction for standard offer customers (id., Vol. 1, at 7). The Settlement includes an accounting of transition costs, a mitigation plan based on divestiture of generation and sale of PPAs, unbundled rates, and provisions for direct access to retail suppliers, universal service, and DSM (id., Vol. 1, at 8-12, 20, 22-24, 26-29, 32-35, Vol. 2, at 54-72). The Settlement does not discuss its impact on employees and communities, but does allow for payments in lieu of property taxes and for employee severance and retraining costs (id., Vol. 2, at 51-52, 56). The Settlement requires Montaup to separate its generation business from its transmission business,[33] in part by selling most or all of its

[33] EECo's distribution business is already separate from Montaup's business.

generation to one or more of a limited number of non-affiliated parties, subject to regulatory approvals (id., Vol. 1, at 5, 32-33; Montaup Divestiture Plan at i, 2).

3. Analysis and Findings

The Settlement provides for retail access on March 1, 1998, as specified in the Act, when retail access is generally available in Massachusetts. The Settlement includes an accounting of stranded costs; a mitigation plan; provisions for a non-bypassable access charge to collect stranded costs, unbundled rates, universal service, and DSM; and provisions to mitigate its impact on employees and communities. The Settlement provides for divestiture by sale of generating assets, accompanied by separate ownership of generation, transmission, and distribution. EECo already owns the distribution assets at net book value, and Montaup already owns the transmission assets at net book value. Recognizing these features, the Department finds that the Settlement is a restructuring plan as defined by the Act.

C. Standard Offer

1. Introduction

The standard offer, besides being a rate schedule, is the mechanism by which several objectives of the Settlement are implemented. The standard offer facilitates (1) the collection of the access charge; (2) the transition to retail competition, through the standard offer power supply auction and the elimination of the wholesale/retail price differential by year four of the standard offer; (3) a price reduction of 10 percent or more for those customers who elect standard offer service; and (4) a limit on the price increases standard offer customers may be exposed to, through the backstop obligation.

The standard offer mechanism proposed by the Company has been the most contested issue in this proceeding (Massachusetts Division of Energy Resources ("DOER") Brief at 5; Attorney General Reply Brief at 2; Indicated Parties Brief at 2; New Energy Ventures (New England) ("NEV") Brief at 1; EECo Reply Brief at 8; Enron Brief at 6). The main issue raised by marketers and third party suppliers is that the proposed structure of the standard offer would inhibit competitors from entering the retail market (Enron Brief at 2-3, 9-10; Indicated Parties Brief at 3-4; XENERGY Brief at 4-6). Marketers and third party suppliers have also raised concerns that Montaup's backstop obligation would allow the Company to procure electricity supplies at costs that are fixed at the wholesale standard offer price (NEV Brief at 2-3; Indicated Parties at 6-7; Enron Brief at 8-13). Marketers and third party suppliers are opposed to the backstop obligation for two reasons. First, they argue that the backstop obligation would guarantee EECo a fixed price for standard offer supplies; this price guarantee is not available to competitive suppliers and, therefore, the guarantee would undermine competition in the market for wholesale supplies for the standard offer service. Second, they argue that the backstop obligation would have the effect of reducing stranded cost mitigation (NEV Brief at 2-3; Indicated Parties at 6-7; Enron Brief at 8-13). Enron, XENERGY, and information obtained from a briefing question have suggested models that would modify one or more aspects of the standard offer. These proposed models and the comments made in response to them are discussed below.

2. Enron's Proposed Model (Elimination of Backstop Service)

Enron proposes to use competitive bidding for the procurement and pricing of standard offer wholesale power, eliminating the wholesale price cap and backstop obligation contemplated by the Settlement (Enron Comments at 16). Under this proposal, EECo would defer underrecoveries between retail standard offer prices and the competitively determined wholesale prices (id.). The 10 percent rate reduction and the stranded cost recovery provided under the Settlement would be retained.

a. Positions of the Parties

(1) Attorney General

The Attorney General contends that Enron's proposal is anti-consumer and that if adopted, it will undermine EECo's willingness to proceed with the Settlement (Attorney General Brief at 15). The Attorney General identifies three major anti-consumer effects of Enron's proposal (id. at 15-16). First, according to the Attorney General, removal of the backstop obligation would subject EECo's customers to the risk of higher surcharges (id. at 15). The Attorney General argues that because the backstop obligation establishes a maximum level of potential deferrals, its removal would expose EECo's customers to an unlimited amount of deferral costs ultimately recoverable through customer surcharges (id. at 15). Next, the Attorney General argues that removal of the backstop obligation would not provide benefits to customers (id. at 15-16). The Attorney General asserts that because competition is not suppressed by the presence of the backstop obligation, its removal would not provide customers with benefits such as more robust competition or reductions in bid prices (id.). Finally, the Attorney General contends that a reduction in stranded cost mitigation due to the backstop obligation is a remote possibility; thus, it would be a reasonable insurance premium to pay to protect consumers from the potential market risks of the backstop obligation (id.).

(2) Division of Energy Resources

DOER's position on Enron's proposal is analogous to that of the Company and the Attorney General based on three major points. First, DOER argues that elimination of the backstop obligation would expose customers to additional risks when compared to the Company's proposal (DOER Brief at 11). DOER contends that if the deferred costs exceed those permitted by the Settlement, customers could be worse off (id. at 14). Second, DOER sees no benefits arising from Enron's proposal in terms of enhanced competitive activity (id.). DOER concedes that removal of the wholesale price cap would encourage greater participation; however, DOER states that such participation would most likely occur in the form of marginal suppliers (id. at 12). DOER is skeptical that these participants would create any perceptible impact on competition (id.). Moreover, DOER asserts that the significant level of interest shown by competitive suppliers in the Massachusetts Electric Company standard offer auction (an auction which contains a backstop obligation identical to that of EECo) is compelling evidence that the backstop obligation is no deterrent to competitive activity (id., citing RR-DPU-11). Finally, with respect to stranded costs and elimination of the backstop obligation, DOER states that the prices paid for Montaup's assets will be based on many factors (id. at 14). DOER contends that potential bidders will realize that the backstop obligation is at most a temporary hindrance, particularly because while the backstop obligation is in effect, the wholesale price ceiling escalates steadily (id. at 14).

(3) Enron

According to Enron, removing the backstop obligation will mitigate adverse effects that customers and competitors would otherwise encounter (Enron Brief at 12-13). In terms of effects on customers, Enron recognizes that the backstop obligation allows EECo to offer power at the standard offer prices (id. at 11). However, Enron contends that customers pay a very high price for the backstop obligation, namely higher stranded costs (id.). Enron claims that removing the backstop obligation will induce higher bids for Montaup's assets, resulting in lower stranded costs (id. at 15, citing Tr. 2, at 35-37, 42-43). In terms of effects on competitors, Enron asserts that market entry, through asset purchases or new construction, will be encouraged by removal of the wholesale price cap, and that wholesale competitors would gain additional flexibility in the management and pricing of their assets (id. at 16, citing RR-DPU-11).[34]

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[34] In Enron's view, removing the backstop obligation is insufficient as a remedy because it does not address retail prices (Enron Brief at 15). According to Enron, standard offer retail prices are "demonstrably below the wholesale cost of power" (id.). Enron (continued…)

(4) Indicated Parties

The Indicated Parties argue that Enron's model would enhance wholesale competition and mitigate stranded costs (Indicated Parties Brief at 6). However, the Indicated Parties assert that, under this model, neither lower energy costs nor lower retail prices would result (id. at 6-8).

(5) New Energy Ventures (NEV)

According to NEV, removing the backstop obligation would enhance wholesale competition (NEV Brief at 2). NEV suggests that the backstop obligation could induce a shortage of electricity in New England because suppliers would choose to sell their power in markets which do not have price constraints (id. at 2-3). NEV asserts that increased stranded cost mitigation is a favorable attribute of Enron's model (id. at 5-6).

NEV argues that implementation of Enron's model would reduce some costs that are ultimately going to be recovered from customers (NEV Brief at 5, citing RR-DPU-12). NEV notes that removal of the backstop obligation would tend to reduce stranded cost deferrals (id.). At the same time, removing the backstop obligation would tend to increase standard offer deferrals (id.). NEV argues that increasing standard offer deferrals while decreasing stranded cost deferrals is a desirable strategy because the carrying costs associated with stranded costs are almost double those of the standard offer (id.). Thus, according to NEV, customers benefit to the extent that stranded cost deferrals can be exchanged for standard offer deferrals (id.).[35]

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[34](…continued)
contends that this price disparity will inhibit the development of retail competition for the first few years of the standard offer (id.). The Department considers arguments related to standard offer retail prices in Section VI.C.3, below.

[35] While NEV notes its support for Enron's model, NEV recommends an additional modification to the Settlement (NEV Brief at 7). NEV asserts that implementation of Enron's model would fail to remedy retail market deficiencies, allowing EECo to maintain dominance in that market (id.). NEV asserts that a comprehensive remedy
(continued…)

(6) XENERGY

XENERGY's position regarding Enron's model is analogous to that of Enron, the Indicated Parties, and NEV, based on two major points. First, XENERGY contends that the backstop obligation will diminish the perceived value of Montaup's generating assets, creating higher stranded costs (XENERGY Brief at 11). XENERGY analyzed the removal of this backstop obligation in terms of stranded costs, projecting an estimated $65.3 million dollar stranded cost reduction based on several assumed values (id. at 16-19). Second, XENERGY asserts that wholesale competition would be enhanced under this model because accurate price signals would be sent (id. at 14). XENERGY claims that the backstop obligation operates as an artificial cap on market prices which will cause decreased supplies and increased demand (id.). In addition, XENERGY notes the effects of the carrying cost differential, and recommends further adjustment to the Settlement to address issues related to retail competition (id. at 11, 19-20, citing RR-DPU-12).

(7) The Company

The Company contends that the backstop obligation is not a barrier to wholesale competition and that it provides benefits to customers (Company Brief at 19, citing RR-DPU-9; RR-DPU-11; RR-DPU-12). In support of these contentions, the Company raises three major points. First, EECo claims that removal of the backstop obligation is unwarranted based on recent actions of numerous market participants (id. at 17, 19, citing RR-DPU-11). EECo notes that in MECo's standard offer auction -- with a backstop obligation identical to that of EECo -- 12 competitive suppliers, including a subsidiary of Enron, were qualified to participate in the final round of bidding on MECo's standard offer load (id.). According to EECo, this response clearly demonstrates that suppliers are willing to supply power at or below the backstop prices

(…continued)

would consist of Enron's model and a mechanism known as a comparability credit (id.). The Department addresses the comparability credit proposal in Section VI.C.3, below.

in today's market (id.; Company Reply Brief at 6). The Company adds that several competitive wholesale suppliers are signatories to its Settlement and MECo's settlement (Company Brief at 13). Second, EECo argues that removal of the backstop obligation would expose its customers to significant new risk (id. at 19). EECo argues that under the backstop obligation, Montaup assumes the risk of wholesale cost increases (id. at 21). According to EECo, Enron's proposal would transfer this risk to EECo customers, and, moreover, EECo customers would be obligated to repay an unlimited level of deferred costs, i.e., deferred costs would not be capped (id.). Finally, EECo disputes the results of XENERGY's quantitative analysis of stranded costs, claiming that the assumptions XENERGY relied on are speculative (Company Reply Brief at 11-12). EECo asserts that Enron's model would have no effect on the level of stranded costs (Company Brief at 7).

b. Analysis and Findings

The Department has three major concerns regarding Enron's model. First, the major premise underlying Enron's model is that it would increase competition at the wholesale level. However, record evidence invalidates assertions that wholesale competition will be dampened by the presence of the backstop obligation and the wholesale price cap. As indicated by DOER and the Company, MECo's standard offer auction with backstop obligations identical to those of EECo generated a significant response by competitive suppliers. In view of definitive evidence based on actual market activity, the Department is hard-pressed to perceive the existence of a wholesale market defect that would justify implementation of Enron's model on these grounds.

Second, in terms of customer impacts, implementation of Enron's model has the potential to burden EECo's customers with higher deferred cost payments. Under standard offer with a backstop obligation, risk of increased wholesale costs is borne by Montaup. In addition, the backstop obligation limits the amount of deferred costs that EECo customers must ultimately repay. In contrast, Enron's model would transfer responsibility for wholesale cost increases to EECo customers and would obligate these customers to repay an uncapped amount of deferred costs. The Department notes that the transfer of responsibility for wholesale cost increases and the removal of the deferral cost cap represents an appreciable increase in risks to be borne by EECo customers. The Department recognizes assertions that wholesale competition would be enhanced with Enron's model, and that this enhancement would benefit customers. However, the Department does not believe that increased risks to EECo customers are justified. As noted by the Attorney General and DOER, discrete customer benefits attributable to Enron's model have not been demonstrated. Moreover, in light of the actual market activity indicated above, the Department sees no competitive basis to justify an increase in risks to be borne by EECo's customers.

Finally, with respect to whether stranded costs would be reduced under Enron's model, the Department notes that this question involves two cost streams and the extent to which these cost streams would be expected to change under Enron's model. Specifically, the two cost streams are (1) deferred wholesale costs, and (2) stranded costs. Enron's model would appear to increase the magnitude of the first cost stream while decreasing the magnitude of the second, suggesting an overall cost reduction. Deferred wholesale costs would be expected to increase because these costs would not be capped; stranded costs would be expected to decrease because the perceived value of Montaup's generating units would be higher without the backstop obligation. Thus, the Enron model suggests that an absolute gain would be created by shifting costs, i.e., swapping stranded costs for deferred wholesale costs. In addition, over time, the value of this cost shift would be expected to grow because the carrying costs of wholesale deferrals are only about one-half that of stranded costs, i.e., 5.0-to-6.0 percent per year versus about 11.5 percent per year.

The Department notes the intuitive merits of Enron's model with respect to stranded costs and total deferred cost reductions. In the abstract, substituting stranded costs for deferred wholesale costs would be expected to create overall cost savings, all else being equal.

The Department believes that this issue lends itself to quantitative analysis; i.e., the two cost streams mentioned above can be estimated with relative ease under a number of plausible scenarios. In addition, since the two cost streams are clearly interrelated, such an analysis should disclose how changes in one cost stream would affect the other. In this respect, the Department notes that the quantitative evidence in support of Enron's model falls short.

XENERGY's quantitative analysis lacks sufficient detail to allow the Department to determine whether this analysis reflects the interrelated nature of the two cost streams. The Department notes that under the Settlement, deferred wholesale costs may be paid down early in the standard offer period. This early payment provision occurs if the proceeds from divestiture exceed Company projections. In other words, to the extent that the divestiture of Montaup's generating assets produces an increment of revenue above Company estimates, the access charge would be reduced accordingly, and this increment of reduction in the access charge would be filled by an equivalent level of deferred wholesale costs so that these costs could be paid down in the early years of standard offer. Thus, if divestiture is favorable, wholesale deferred costs are not carried across time at their maximum level; some of these costs are paid down early to the extent allowed by a favorable divestiture. While XENERGY's analysis included favorable divestiture proceeds in the amount of $65.3 million dollars, it is not clear that XENERGY's analysis provided for any corresponding reduction in wholesale deferred costs consistent with the early payment provisions. Such an omission would overstate the benefits of Enron's model and call into question XENERGY's claimed 25 percent reduction of total deferred costs. In addition, as pointed out by the Company, XENERGY's quantitative analysis assumes a carrying cost for deferred wholesale costs that is several points higher than that indicated in the Settlement, and XENERGY's analysis assumes a wholesale market price that remains higher than standard offer retail prices throughout the entire seven-year standard offer period. The Department notes that these assumptions have the tendency to overstate the potential benefits of Enron's model. A stronger analytic presentation would have included a sufficient level of explanation and additional outcomes based on a range of plausible assumptions. Without such an analytic presentation, the Department lacks the information necessary to allow a meaningful evaluation of claims regarding this issue.

Accordingly, based on the foregoing, the Department finds that Enron's model should not be adopted.

3. XENERGY's Model (Comparability Credit)

a. Introduction

In this section, the Department evaluates an adjustment to the Settlement proposed by XENERGY. In XENERGY's view, EECo's standard offer pricing displays anti-competitive tendencies that will preclude development of a competitive retail marketplace for several years (Exh. XENERGY-15, at 3). XENERGY recommends an adjustment to the Settlement intended to neutralize such tendencies (id.).

XENERGY identifies three anti-competitive elements of EECo's standard offer: (1) EECo will sell standard offer power below its cost of acquisition; (2) EECo will avoid financial losses normally expected from below-cost sales; and (3) EECo's standard offer prices are too low, i.e., below the expected market prices (Exh. XENERGY-15, at 3-4). XENERGY contends that, because of these elements, competitive retail suppliers cannot compete on an equal footing with EECo (id. at 4). Moreover, XENERGY asserts that EECo will secure an insurmountable competitive advantage in the retail market unless competitive retail suppliers receive equal treatment (id. at 3).

Accordingly, XENERGY proposes a comparability credit, or a deferral mechanism comparable to the deferral arrangement provided to EECo under the standard offer (Exh. XENERGY-15, at 7). Under XENERGY's comparability credit, the scope of the deferral arrangement proposed by EECo to apply only to standard offer transactions would be expanded to include all retail transactions (id.). For example, if EECo were to defer 0.4 cents per KWH in 1998 (based on the standard offer wholesale cost of 3.2 cents per KWH and the standard offer retail price of 2.8 cents per KWH) then all competitive retail transactions would be granted a 0.4 cent per KWH deferral in that year (id. at 7).[36] Under XENERGY's model, the resultant deferrals would be accumulated for eventual recovery under the same terms and conditions proposed to govern EECo's standard offer deferrals (id.).

b. Positions of the Parties

(1) Attorney General

The Attorney General argues that XENERGY's comparability credit proposal should be rejected (Attorney General Brief at 18-20). The Attorney General contends that there is no validity to the claims that standard offer pricing is too low and that the standard offer will inhibit the development of a competitive market (Attorney General Reply Brief at 4). In support of these contentions, the Attorney General asserts that (1) evidence to predict future market prices is absent from this record; therefore, XENERGY's claims regarding future market prices are unsupported; (2) in the past, a competitive supplier sold power at retail profitably at 2.1 cents per KWH, and XENERGY priced retail power below the standard offer price without a comparability credit; and (3) XENERGY testified that the comparability credit would have no effect on energy prices (Attorney General Brief at 18-20, citing Exh. AG-1, Tr. 4, at 31-33; Attorney General Reply Brief at 4-5).

The Attorney General argues that EECo's standard offer should be adopted for the reasons stated in Massachusetts Electric Company, D.P.U. 96-25 (1997); i.e., because EECo's standard offer (1) assures a discount for all customers; (2) avoids placing customers in the position of having to exercise choice immediately; (3) contains incentives to promote acquisition of power at the lowest possible cost, thereby fostering competition in the bulk power market; and (4) expands the scope of retail competition based on progressively

[36] Under XENERGY's comparability credit, if a competitive retail supplier were to sell power at 3.0 cents/KWH, the customer would pay the supplier 2.6 cents/KWH, EECo would pay the competitive retail supplier 0.4 cents while accumulating this payment as a deferral, allowing the competitive retail supplier to receive 3.0 cents/KWH.

escalating retail prices; thus curing, over time, any impairment to competition (Attorney General Reply Brief at 5, citing D.P.U. 96-25, at 25-26). Moreover, the Attorney General asserts that the Department's standards of conduct will prohibit the Company from promoting the services of any affiliate including a competitive entity (id. at 5, citing 220 C.M.R. § 12.03(11)).

(2) Division Of Energy Resources

DOER argues that XENERGY's proposed comparability credit will increase costs to customers and that it is incompatible with the Settlement (DOER Brief at 21). First, with respect to increased costs, DOER asserts that the comparability credit would assure deferrals for EECo's entire load, irrespective of customer migration from standard offer to a competitive option (id.). DOER states that this blanket approach would add deferral costs that must be ultimately repaid by customers (id.). Second, DOER maintains that XENERGY has failed to demonstrate that the comparability credit would provide tangible net benefits to customers (id. at 22). DOER notes that XENERGY's witness testified that the availability of the comparability credit bears no relationship to the cost at which the competitive supplier acquires power in the wholesale market or the ultimate price charged to customers at retail (id. at 21-22, citing Tr. 4, at 145). Further, according to DOER, the comparability credit may result in a perverse pricing arrangement (id. at 22). DOER recounts that the amount of the comparability credit, in terms of cents-per-KWH, would be established at the time of standard offer auction (id. citing Tr. 4, at 143-144). Once this amount has been established, it would remain fixed going forward in time (id.). Consequently, even if wholesale prices were to fall at a future point, as a fixed amount the comparability credit would not adjust to such circumstances (id.). DOER points out that under such conditions competitive retail suppliers would nonetheless continue to receive the comparability credit, adding to deferral costs that customers would have to repay (id.). Finally, DOER concludes that the comparability credit is an unattractive option because the intangible benefits of potentially more robust retail competition in the first few years of retail choice would come only at very tangible additional expense to the customers that competition was intended to benefit (id. at 22).

With respect to claims that the standard offer would provide EECo with an unfair competitive advantage, DOER argues that such claims are misguided (DOER Brief at 8). DOER asserts that the standard offer is not a competitor in the marketplace but rather a rate subject to regulatory approval (id. at 5, 8). DOER asserts that there is no profit to EECo in retaining standard offer load; that EECo will not market standard offer service; and that EECo may not offer standard offer service to new customers, nor may it vary standard offer prices for purposes of customer retention (id. at 8). Finally, DOER anticipates that competitive retail suppliers will seek to lure customers from standard offer service with the introduction of new products of which generation is but one component (id., citing Tr. 4, at 139). For example, DOER expects competitive retail suppliers to offer numerous combinations of energy efficiency, generation, and non-energy products (id. at 23, citing Tr. 1, at 136). DOER notes that EECo's standard offer would provide no similar product combinations (id. at 8).

(3) Enron Capital and Trade Resources

Enron urges the Department to reject the Settlement because, in its view, EECo's standard offer is so flawed that it will impair the competitive market and defeat the fundamental purpose of industry restructuring (Enron Brief at 8). Enron asserts that the comparability credit should be adopted to bolster retail competition in the early years of standard offer service, even though Enron does not believe that the comparability credit is the best solution to problems with EECo's standard offer (id. at 22).

(4) Indicated Parties

Generally, the Indicated Parties contend that the standard offer's below-cost pricing and deferral mechanisms will obstruct the development of retail competition (Indicated Parties Brief at 7-8). However, the Indicated Parties take no position with respect to XENERGY's comparability credit (id. at 2-3).

(5) New Energy Ventures

NEV argues for implementation of the comparability credit based on three major points (NEV Brief at 1, 9, 12-13). Specifically, NEV claims that (1) the standard offer is demonstrably underpriced in its early years; (2) the comparability credit would nullify any undue competitive advantage associated with this underpricing, allowing a robust competitive retail market to develop; and (3) EECo's current standard offer deferral mechanism may harm the most vulnerable customers (id.).

NEV argues that the record in this proceeding clearly demonstrates that standard offer retail prices for 1998-2000 will be substantially below competitive retail and even wholesale prices (NEV Brief at 10-11). In support of this argument, NEV relies on the testimony of XENERGY's witness, Mr. Walker, and on a DOER memorandum which proposed a levelized avoided generation component of 4.0 cents per KWH (Tr. 4, at 32; NEV Brief at 10-11, citing Exh. ECT-11). In addition, NEV contends that, in contrast to EECo's standard offer, competitive retail suppliers have no ability to defer losses with a guarantee of eventual recovery (NEV Brief at 11-12). Thus, NEV argues that, in EECo's service territory, the standard offer's underrecovery and deferral mechanisms will deny entry to competitive retail suppliers during the first three years of the standard offer period (id.). With respect to customer harm, NEV argues that the standard offer may encumber small customers with deferral costs left behind by large customers (id. at 12-13). NEV envisions that if large customers migrate from standard offer service after taking such service in the early years, their deferral costs would be borne, in the first instance, by the customers remaining on standard offer service (id.). NEV anticipates that the customers most likely to remain on the standard offer at that point would be residential and small commercial customers (id.).

(6) The Company

EECo maintains that XENERGY's comparability credit proposal is profoundly flawed and that the record provides no basis to indicate that it is needed (Company Brief at 14-17, 27-28). EECo further maintains that its standard offer is reasonable and that it should be implemented without adjustment (id. at 12-18).

EECo argues that the comparability credit is inadequate as a means of establishing a level playing field with respect to standard offer prices (Company Brief at 27-28). EECo asserts that the comparability credit would likely undercut or overshoot, rather than level, the playing field (id. at 27). According to EECo, if 0.4 cents were to be deferred under the standard offer and a competitive retail supplier were to sell power at 3.0 cents per KWH, then under the comparability credit, the customer would pay the competitive retail supplier 2.6 cents per KWH, and EECo would pay the competitive retail supplier 0.4 cents and defer 0.4 cents (id. at 28). In this example, a competitive retail supplier would exceed equality on the playing field and actually undercut the standard offer with the comparability credit (id.). In another example, if a competitive retail supplier were to sell power at 4.0 cents, then the customer would pay the supplier 3.6 cents, with EECo paying out and deferring 0.4 cents (id. at 28-29). In this instance, EECo anticipates no meaningful effect from the comparability credit because the retail supplier would not be competitive even with the comparability credit (id. at 28-29). EECo suggests that the comparability credit is a subsidy for competitive retail suppliers, offering no assurance that a level playing field will result from its implementation (id. at 30). EECo adds that the comparability credit would simply increase deferral costs without providing any tangible benefits (id. at 29).

With respect to the concern that the standard offer will be offered at prices that are going to be below the market prices, EECo argues that the evidence in this record is insufficient to support a finding that market prices are prohibitively high or that market prices will be higher than standard offer prices for any length of time (Company Brief at 14-17;

Company Reply Brief at 13-17). According to EECo, none of the evidence on this point is persuasive (id.). With respect to XENERGY's claim that it was unable to procure power at prices low enough to compete with standard offer prices, EECo argues that because XENERGY represents a particular type of marketer, i.e., one that buys and resells power but owns no generation, XENERGY's experience by itself is inadequate to support any conclusions suggesting a widespread mismatch in prices (id. citing Tr. 4, at 32). With respect to a LaCapra Associates ("LaCapra") study cited by Enron in support of its contention that market wholesale prices would be greater than 4.0 cents per KWH, EECo argues (1) even though the New Hampshire Public Utility Commission ("NHPUC") reviewed this study, the NHPUC made no finding to suggest that market prices will be at the levels indicated by the LaCapra study; and (2) the NHPUC criticized the LaCapra study in certain respects, primarily because its price projections might be too high and because it failed to recognize the potential for "certain large suppliers with good cash flows to lower market prices in an effort to buy market share" (Company Reply Brief at 15, citing Exh. ECT-1, at 80). With respect to DOER's memorandum which proposed a levelized avoided generation component of 4.0 cents per KWH, EECo points out an explicit caveat stated in this memorandum: "We strongly emphasize that the component should not be regarded as a proxy for market price, but rather as a value to apply *for the purposes of DSM planning, evaluation, and implementation only*" (emphasis in original) (Company Brief at 16, citing Exh. Enron-11, at 2-3). According to EECo, this caveat indicates that the avoided generation component found in DOER's memorandum is clearly unsuitable for use as an indicator of future market prices (id.). Moreover, EECo asserts that its standard offer would be appropriate even if market prices were high (id. at 18). EECo suggests that, by definition, there can be no near-term rate relief unless the standard offer is priced below market, irrespective of the particular market price level (id.).

With respect to claims that the standard offer will prevent the development of retail competition, EECo argues that the standard offer is intended to be a transitional mechanism, not a competitive supply option (Company Reply Brief at 4). EECo contends that the purpose of the standard offer is to establish a price path toward competition that is fixed, predictable, and at a level that will guarantee EECo customers an initial 10 percent discount (id. at 12).

In support of its view that the standard offer is designed as a transitional mechanism, EECo recounts the major characteristics of standard offer (Company Brief at 4-7). EECo notes that (1) standard offer retail prices will escalate at about 10 percent per year, encouraging customer migration from the standard offer to competitive alternatives; (2) standard offer prices are not adjustable, in contrast to competitive suppliers' prices which can be modified in response to customer needs and marketing opportunities;[37] and (3) standard offer has been established in recognition that some customers will not be ready to take advantage of the competitive market immediately, necessitating a transition mechanism (id. at 16, 29-30; Company Reply Brief at 6, 21, 18-19).

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[37] EECo argues that it is not, and cannot be, a competitor in the retail marketplace (Company Reply Brief at 17-18). EECo notes that following industry restructuring it will operate as a regulated distribution company supervised by the Department (id.). Thus, according to EECo, the Department will regulate its rates and the Department's Standards of Conduct will govern its conduct, prohibiting the sharing of any advantage with a competitive affiliate (id.).

c. Analysis and Findings

Section 308 of the Act requires that, if and to the extent that retail prices for standard offer power are below the wholesale costs of standard offer power, then the Department shall investigate whether it is appropriate to extend, through new legislation, a comparability credit to non-standard offer customers. XENERGY asserts that record evidence regarding EECo's standard offer pricing activates a statutory obligation on the Department under Section 308 of the Act to commence an investigation into the appropriateness of amending the Act to provide for a comparability credit (XENERGY Legislative Comments at 3-6, citing the Act, Section 308). The Department will monitor the relationship between standard offer prices and wholesale costs and will initiate an investigation in the future if circumstances trigger Section 308 of the Act.

However, in this proceeding, the Department states its concerns regarding particular aspects of XENERGY's comparability credit. First, the Department notes that implementation of the comparability credit would create higher deferred costs. Because every transaction in EECos' service territory would be eligible for the comparability credit, deferred costs would accumulate regardless of customer migration from standard offer to competitive options. Second, as noted by DOER, the comparability credit, once established, would remain fixed even if market prices declined to the point where the comparability credit was no longer necessary. Thus, customers would be subject to deferral costs even if market conditions were such that the comparability credit was not needed. Finally, as noted by the Attorney General and DOER, XENERGY indicated that the availability of the comparability credit would bear no relationship to the cost at which the competitive supplier acquires power in the wholesale market or the ultimate price that would be charged to retail customers. Thus, it is questionable whether the comparability credit would provide tangible benefits from a customer perspective. Based on the foregoing, the Department fails to perceive that the comparability credit would provide a level of benefits commensurate with the costs that EECo customers would absorb under an implementation of the comparability credit.

A key substantive issue raised in this proceeding concerns whether EECo's Standard offer prices will be below market prices at the time of retail access. While a number of parties have argued that the record demonstrates that standard offer prices are going to be below market prices, the Department notes that the evidence used as the basis for this argument has significant flaws. The record evidence on this issue is weak because of the explicit disclaimers and criticisms made by the originators of the documents relied on. In the absence of stronger, more definitive evidence, the Department does not believe that the necessary burden of proof has been met on this issue.

Finally, the Department agrees with the Attorney General, the DOER, and the Company with respect to the transitional character of standard offer. Consistent with principles developed in earlier restructuring proceedings, the Department believes that the standard offer represents an important and necessary step towards development of a competitive retail market. D.P.U. 96-100, at 135-138; Electric Industry Restructuring, D.P.U. 95-30, at 45 (1995). Further, the standard offer is the means by which a rate discount has been assured for EECo customers. The Department notes that, in comparison to the standard offer, competitive suppliers will enjoy many advantages associated with superior flexibility, including innovation, pricing adjustments, and product combinations.

In sum, the Department notes that the comparability credit would add costs without providing a commensurate level of benefits, that evidence in this record does not support a finding regarding the future market price of power, and that EECo's standard offer represents a reasonable transitional mechanism. Accordingly, based on the foregoing, the Department finds that XENERGY's comparability credit should not be adopted.

4. Briefing Option (Elimination of the Standard Offer Deferral and Reduction of the Access Charge)

a. Introduction

An option proposed in a briefing question ("briefing option") was introduced by the Department to broaden the discussion regarding the structure of the standard offer. The briefing option would operate in two stages (Department Briefing Question 2). From 1998 through 2000, the retail standard offer price would be set by competitive bid, but limited by the wholesale price cap (id.). The Access Charge would be set at a level such that the sum of the standard offer price and the Access Charge would be equal to the sum of those two charges under the Settlement (id.). From 2001 to 2004, the standard offer prices and Access Charge would be as they are set in the Settlement, unless the Access charge can be reduced by mitigation of stranded costs (id.).

b. Positions of the Parties

(1) Attorney General, DOER, The Company

The Attorney General, DOER and the Company concur that the briefing option should be rejected (Company Brief at 24, citing Tr. 3, at 229-231). They contend that this approach would substantially alter the terms of the Settlement because of the change in balance between the access charge and the standard offer (Attorney General Brief at 16; DOER Brief at 17; Company Brief at 25). According to the Company, the approval of a settled schedule for stranded cost recovery is of critical importance because the Company's restructuring and divestiture plans, financing requirements and FERC approval, are contingent on a determined recovery of stranded costs (Company Brief at 25-26). DOER points out that implementation of the briefing option could result in a decrease in the fixed component of stranded cost recovery of up to 30 percent in the first three years of the standard offer (DOER Brief at 17). The Attorney General, DOER, and the Company maintain that customers would be harmed by the implementation of this approach because it decreases stranded cost recovery in the early years and increases stranded cost recovery in later years (Attorney General Brief at 17; DOER Brief at 18; Company Brief at 24). The Attorney General and DOER point out that the deferral of stranded costs will accrue carrying costs at a rate significantly higher than the rate for standard offer deferrals, because the rate applicable to deferred access charges is 11.544 percent, while standard offer deferrals would accrue interest at the two-year Treasury Bill rate (Attorney General Brief at 17; DOER Brief at 18).

(2) Enron, Indicated Parties, NEV, XENERGY

Enron, Indicated Parties, NEV and XENERGY are generally in favor of the briefing option (Enron Brief at 19; Indicated Parties Brief at 10; NEV Brief at 7; XENERGY Brief at 22). However, NEV and XENERGY admit that adopting the briefing option would fundamentally change the Settlement terms and they posit that the comparability credit would be able to address competitive concerns without fundamentally changing the Settlement (NEV Brief at 8; XENERGY Brief at 23-24). Enron asserts that while this approach would bring about some competitive benefits in the first few years, the benefits would be limited because the backstop obligation is retained (Enron Brief at 19). Indicated Parties recommend adoption of the briefing option, with the provision that the method of pricing for the first three years be maintained throughout the transition period (Indicated Parties Brief at 10). While Enron does not view the recovery of stranded costs in this approach as having the potential to cause financial uncertainty for EECo, NEV expresses the opposite sentiment (Enron Brief at 21; NEV Brief at 8). NEV and XENERGY assert that because the briefing option would fundamentally change the Settlement, the comparability credit is a better alternative to address competitive concerns (NEV Brief at 8; XENERGY Brief at 23). XENERGY acknowledges that the briefing option may be easier to administer than the comparability credit model, but according to XENERGY, the briefing option does not take into account overhead administrative costs incurred by marketers, because the wholesale price would equal the retail price (XENERGY Brief at 23).

c. Analysis and Findings

The Department introduced the briefing option to the discussion on the structure of the standard offer in an effort to analyze the various modifications being proposed by the intervenors in the broader context of a variable access charge. The Department has reviewed the evidence and argument to determine whether the changes proposed by this approach would be in the public interest. The Department finds that the briefing option does not contribute to both competitive retail and wholesale markets. The briefing option is focused exclusively on the retail standard offer prices. Therefore, any potential benefits of the briefing option would be limited in their scope. The Department also finds that making the access charge variable could delay the Company's recovery of stranded costs and result in deferrals that have higher carrying costs. In its guidelines for standard offer service in D.P.U. 96-100, at 137, the Department stated that the provision of standard offer service should not result in additional stranded costs for distribution companies. The Department recognizes that a variable access charge in the initial period of the standard offer could result in lower than projected recovery of stranded costs. The Department also notes that the briefing option would result in a fundamental alteration of the existing Settlement in a manner that may jeopardize the agreement itself. In view of these arguments, the Department finds that the adoption of the briefing option would not bring substantive additional benefits to the current proposal.

5. Conclusion on Pricing of Standard Offer

Section 193, Subsection 1B(b) of the Act requires that a distribution company provide a standard service transition rate for the period from March 1, 1998, to January 1, 2004, at prices and terms approved by the Department. The Department notes that the Company has agreed to provide standard offer service to its customers beginning on March 1, 1998, and that the prices and terms of the Company's standard offer service proposal are subject to approval by the Department.

XENERGY claims that Section 193, Subsection 1C(ii) of the Act requires EECo to sell its standard offer power to new entrants, on the sole condition that the power be resold to customers within EECo's service territory (XENERGY Legislative Comments at 6-10).[38] XENERGY contends, among other things, that under this provision of the Act, EECo's standard offer (1) is a service, (2) must be made available to all customers and suppliers simultaneously, and (3) must be made available on a comparable basis (XENERGY Legislative Comments at 6-11, citing the Act, Section 193, Subsection 1C(ii)).

The Department notes that, as a general matter, sales for resale generally fall under the authority of FERC. Thus, as a sale for resale, XENERGY's proposal lies outside the scope of the Department's authority. In addition, with respect to the Act, the Department notes a clear distinction with respect to "customers" and "suppliers" in terms of products, services, discounts, rebates, and fee waivers ("products") offered by a distribution company. In the Department's view, the Act should not be read to suggest that every product offered to a customer must also be offered to a supplier, but instead, that a product offered by the distribution company to any of its customers must be offered to all of its customers, and, similarly, that a product offered by the distribution company to any supplier must be offered to all suppliers. The Department believes that logic supports our reading of the Act; otherwise, a distribution company would be required to offer every retail product, including DSM to suppliers. Accordingly, based on the foregoing, the Department finds that the Company's standard offer proposal substantially complies or is consistent with the Act.

The Department notes that responsibilities for providing standard offer service in a restructured industry have been assigned to distribution companies. D.P.U. 96-100, at 137. In making this assignment, the Department provided distribution companies with a high degree

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[38] Xenergy referenced the following provision of the Act: "(ii) all products, services, discounts, rebates, and fee waivers offered by a distribution company shall be available to all customers and suppliers simultaneously, to the extent technically possible, on a comparable basis;" Section 193, Subsection 1C(ii) of the Act.

of flexibility, such that distribution companies could make standard offer service proposals that would best suit their particular situations. Id. at 137. Notwithstanding this flexibility, the Department also established certain basic requirements applicable to standard offer service proposals, including the following: (1) a standard offer service must provide near-term rate relief; (2) no additional stranded costs must result from a distribution company's provision of standard offer; and (3) a decision by a distribution company to arrange for standard offer generation with an affiliate would be undertaken at the risk of shareholders. Id. at 137-138. Moreover, the Department recognized that its framework for standard offer service would essentially establish price cap ratemaking for such service. Id. at 138.

In this proceeding, the Department has been presented with four standard offer proposals, i.e., the Company's, Enron's, XENERGY's, and the briefing option. In conducting its review of these proposals, the Department has addressed a broad range of issues reflecting the key components of each particular proposal. Based on these reviews, the Department has found deficiencies with respect to Enron's model, XENERGY's comparability credit, and the briefing option. The Department has found no commensurate deficiencies the Company's standard offer. Moreover, because the Company's standard offer best approximates the Department's framework for standard offer service as indicated in D.P.U. 96-100, and because, as a product of the settlement process, the Company's standard offer represents a balance among competing interests, the Department finds that the Company's proposal is consistent with Department precedent and the public interest. Accordingly, the Department approves the Company's standard offer proposal.

6. Standard Offer Auction

a. Introduction

The Settlement provides for standard offer service supplies to be sought from marketers and third party suppliers through an auction, with a price ceiling for standard offer service supplies established by the wholesale prices that have been guaranteed by Montaup. EECo's has designed its auction to consist of a two-stage process: a Seven Year Flat Discount Auction followed by an Alternative Individual Year Auction. Bidders are required to make a refundable deposit of $5,000 per megawatt ("MW") for each year the bidder proposes to supply power for standard offer service. Additionally, winning bidders would be required to establish a performance bond in the amount of $50,000 per MW for each year the bidder proposed to supply power for standard offer service. According to the Settlement, the Company intends to issue the final request for proposals ("RFP") for standard offer service at the time that the purchase and sale agreements for Montaup's interest in the Somerset Station and Canal 2 have been executed, but no later than six months after the retail access date.

b. Positions of the Parties

(1) Enron

Enron raises issues with respect to the bidding process for the Company's securing standard offer service (Enron Comments at 18; Enron Brief at 26-27). Enron points out that both the bid deposit and the performance bond required by EECo in the proposed standard offer RFP have been set too high and would result in few bidders for standard offer supply (Enron Comments at 18-19; Enron Brief at 26). Enron also contends that EECo has not explained how it plans to serve its standard offer customers during the estimated eight-month period from the commencement of retail access to the date when suppliers are selected (Enron Brief at 27).

(2) The Company

The Company states that elements of its standard offer auction, including the bid deposit and performance bond amounts, is currently under review (Exhs. DPU-45; Enron-10). The Company anticipates discussing modifications to the auction with Settlement parties (Exh. DPU-45).

c. Analysis and Findings

Section 193, Subsection 1B(b) of the Act requires a distribution company to purchase electricity after a competitive bid process that is reviewed and approved by the Department.

The Company has proposed a two-stage auction process that is designed to enable third-party bidders to compete for a number of short- and long-term supply options. In addition, the Department notes that, even though the Company may continue to refine certain details associated with its bid process, the Company is nonetheless committed to implementing a competitive auction for its supplies of standard offer power. Accordingly, the Department finds that the Company's standard offer auction proposal substantially complies or is consistent with the Act.

The Department recognizes Enron's concerns with respect to the bid deposit, the performance bond, and the period between the commencement of retail access and the date when standard offer suppliers are selected. The Department notes that EECo proposes to continue to refine the details of its auction process in concert with the Settlement parties. Accordingly, based on the foregoing, the Department approves the Company's standard offer auction.

7. Transferability of Standard Offer Service

a. Introduction

Although the initial Settlement proposal omitted provisions regarding transferability, i.e., whether a customer may relocate within the Company's service territory and still retain standard offer service, Revisions permit such transferability for all EECo customers (Exh. EECo-2).

b. Positions of the Parties

The Attorney General interprets the Settlement to allow transferability and suggests that the Department codify this interpretation in its Terms and Conditions docket, D.P.U. 97-65

(Attorney General Brief at 20).[39] DOER interprets the Settlement to preclude transferability, because transferability would decrease customer migration from standard offer service, delaying competition (DOER Brief at 24). However, DOER suggests that transferability be permitted for residential customers, including low-income ones, to minimize customer confusion (id.). EECo indicates that it can manage transferability with little added expense and little impact on load (EECo Brief at 31). EECo's Revisions allow transferability, and EECo also suggests that the Department set up rules regarding transferability in D.P.U. 97-65 (Exh. EECo-2; EECo Brief at 31-32).

c. Analysis and Findings

Section 193, Subsection 1F(4)(iii) of the Act requires that a residential customer eligible for low-income discounts receiving standard offer service be allowed to retain standard offer service upon moving within the service territory of a distribution company. The Department notes that EECo's Revisions regarding transferability of standard offer service extends to all EECo customers, including residential customers eligible for low-income discounts. Accordingly, the Department finds that the Company's proposal regarding transferability of standard offer service substantially complies or is consistent with the Act.

The Department finds that allowing transferability, including the Revision's extension of transferability to all customers, is consistent with the Department's restructuring principle of minimizing customer confusion.

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39 On June 13, 1997, the Department initiated a proceeding to develop model terms and conditions governing the relationships between distribution companies and customers, and distribution companies and competitive suppliers. Notice of Inquiry and Order Seeking Comments on Model Terms and Conditions for Distribution Companies, D.P.U. 97-65 (June 13, 1997).

D. <u>10 Percent Rate Decrease</u>

1. <u>Introduction</u>

The Settlement provides for a 10 percent rate decrease, based on a comparison of the Settlement rates with the base rates and conservation charges in effect during October 1996, and the average fuel costs for the twelve-month period ending June 30, 1996 of 1.889 cents per KWH, with the proposed standard offer service tariffs and standard offer price of 2.8 cents per KWH (Exh. EECo-1, Vol. 1, at 203, 288-318). The standard offer price is subject to adjustment and is scheduled to increase gradually to 5.1 cents per KWH by the year 2004 (<u>id.</u> at 209). Actual prices will also depend on the success of mitigation efforts, a fuel price index, a 6.0 percent floor and an 11.0 percent to 12.5 percent ceiling on EECo's return on equity, and changes in accounting standards or tax laws, as well as future electricity commodity prices for those who choose to leave standard offer service (<u>id.</u> at 7-12, 20-23). The Settlement incorporates revised conservation charges, resulting in an annual revenue increase of $1,526,500 over the rates in effect during October 1996. <u>See</u> Section IV.C, above.

2. <u>Positions of the Parties</u>

a. <u>Low-Income Intervenors</u>

The LII argue that the 10 percent rate decrease claimed under the Settlement is deceptive because the pre-Settlement rates are higher than they would have been in the absence of the Settlement (LII Brief at 1; LII Legislative Comments at 4). According to the LII, the current rates include $4,182,899 in conservation charge overrecoveries for 1996, which under traditional ratemaking practice would have been returned to ratepayers (LII Brief at 1, <u>citing</u> Exh. LII-4; RR-LII-1). The LII further contend that current rates include a 1997 conservation charge overrecovery being retained by the Company, a $6,537,998 PCAC refund from Montaup, and the creation of a new storm fund (LII Brief at 1, <u>citing</u> Exhs. LII-12; LII-13; LII-14; RR-LII-7; LII Legislative Comments at 4).

In addition, the LII argue that the Settlement imposes no obligation on the Company to maintain the rate reduction, which the LII says could last as little as one day before being subject to assorted adjustments for rate of return, accounting and tax changes, fuel costs, and deferred charges (LII Brief at 1, citing Exhs. LII-2; DPU-15). The LII also argue that experience in other deregulated industries demonstrates that suppliers will attempt to segment the market such that prices could increase to certain classes of customers under the Settlement (LII Brief at 1). They fault the Settlement for its failure to set forth a mechanism to identify the unintended consequences of competition and to address those problems (id.).

b. Attorney General

The Attorney General contends that the Settlement substantially complies with the Act (Attorney General Legislative Comments at 1). According to the Attorney General, the Settlement will in fact result in a 10 percent reduction for all customers in the price of electric service, and will limit future increases in such a way that the "real," i.e., inflation-adjusted, value of these savings, relative to the current regulatory framework, is maintained through the year 2004 (Attorney General Brief at 10). The Attorney General asserts that the 10 percent decrease is based on the base rates and conservation charges in effect during October 1996, and the average fuel costs for the twelve-month period ending June 30, 1996 (id.).

The Attorney General states that the LII are incorrect in their claims that certain provisions in the Settlement create the potential to impair the value of the savings resulting from the initial price reduction (id.). The Attorney General argues that the provisions providing for automatic adjustments to recognize significant accounting and/or tax changes as well as increases in the cost of fuel, provide for recognition of costs beyond the utility's control, and that these costs are passed through routinely under traditional cost-of-service regulation (id. at 11). Therefore, the Attorney General contends that allowing adjustments for these costs merely provides that post-1998 prices will at most track at a lower level those that would otherwise occur under the current regulatory framework (id.).

With respect to the rate of return adjustment provision, the Attorney General claims that it is highly unlikely that the Company's return on equity would fall below six percent during the term of the Settlement (id. at 11-12). Even if such an event were to occur, the Attorney General states that the value of the savings achieved under the Settlement would be impaired only if (1) the magnitude of the earnings shortfall were unprecedented, and (2) the proceeds from the divestiture of Montaup's non-nuclear assets were some "meaningless fraction" of the underlying book value (id. at 12). The Attorney General also posits that with lower electricity prices and the deregulation of the generation market, usage can be expected to increase beyond current forecasts and, thus, provide greater earnings to the Company (id.).

Additionally, the Attorney General notes that the conservation charge overrecoveries are being used to prefund the increased DSM and renewables funding, which will increase from the current 1997 budget of $6,484,500 to $10,400,000 in the year 2001, and include provisions to target low-income customers (id., citing Exh. EECo-1, Vol. 1, at 26-27). The Attorney General contends that these increases are made possible only through pre-funding, and that the increased programs will serve to benefit low-income customers in a manner far greater than the initial 10 percent rate reduction under the Settlement (Attorney General Brief at 12).

c. The Company

The Company contends that the Settlement is in substantial compliance with the Act (Company Legislative Comments at 2, 5). EECo maintains that the Settlement's standard offer provisions are consistent with the initial 10 percent rate reduction mandated under the Act, and that this reduction, in combination with the net proceeds from divestiture and the net savings from securitization, will produce the 15 percent rate decrease required under the Act by September 1, 1999 (id. at 5).

The Company argues that the LII have selectively cited provisions of the Settlement in their criticism of the rate reduction (Company Reply Brief at 24). EECo contends that the LII fail to consider the benefits of the base rate freeze under the Settlement, and notes that certain of the cost increase components deal with costs that should be borne by all customers in any event (id.). The Company states that the Settlement is a delicate balancing of numerous competing issues, which provides customers maximum rate relief while continuing to address the interests of the individual parties, as well as public policy concerns (id.).

3. Analysis and Findings

Section 193, Subsection 1B(b) of the Act requires that the standard service transition rate, combined with other charges, must provide an overall rate reduction of 10 percent over rates in effect during August 1997, or such other date as the Department determines to be appropriate. Subsection 1B(b) also provides that distribution companies provide by September 1, 1999, through a combination of the 1998 rate reduction, net proceeds from divestiture, and net savings through securitization, an overall rate reduction of 15 percent over inflation-adjusted August 1997 rate levels, or other such date as the Department may determine. Additionally, Section 315 of the Act requires electric or gas distribution companies to furnish gas or electricity to persons or corporations engaged in the business of agriculture or farming at a rate set at least an additional 10 percent below any other rate, price, or charge category.

The Settlement provides for a rate decrease of 10 percent over the combined base rates and conservation charges that were in effect during October 1996, and the average fuel costs for the twelve-month period ending June 1996. The Company's fuel adjustment clause ("FAC") factor for the month of August 1997 was $.02249 per KWH, which is greater than the FAC factor used in the Settlement. Eastern Edison Company, D.P.U. 97-4B at 5 (1997). Because of the higher FAC factor in effect during August 1997, the retail access rates constitute a greater reduction than used for reference purposes in the Settlement, and therefore a greater reduction than the 10 percent required under the Act.[40] Moreover, as the Company correctly notes, nothing in the Settlement precludes EECo from implementing the additional 5 percent rate decrease required under the Act by September 1, 1999, through a combination of divestiture and securitization.

The Settlement is silent with respect to the additional 10 percent discount provided to agricultural customers. The Department understands that the settling parties could not have been aware at the time of negotiations that the various legislative initiatives under consideration would make specific provision for agricultural customers. The Department will address this issue as part of its promulgation of final rules in D.P.U. 96-100. Accordingly, the Department finds that the Settlement substantially complies or is consistent with the Act.

In addition to the 10 percent rate decrease to take effect upon retail access, the Settlement provides for revised conservation charges that take effect upon approval of the Settlement. While some rate classes will experience conservation charge reductions as of the date of this Order, most rate classes will experience conservation charge increases that vary by customer class. This includes low-income customers on Rate R-2, who will experience a rate increase of approximately 1.1 percent over rates in effect during August 1997, before a rate decrease of about 13 percent from August 1997 levels takes effect on March 1, 1998. These increases, as well as the Settlement's treatment of the 1996 and 1997 conservation charge overcollections and 1996 Montaup PCAC refund, provides a mechanism through which the Company may embark on an expanded DSM and renewables program. The Department finds that the expanded DSM program is consistent with one of the Department's conditions for facilitating a restructured electric industry, i.e., the maintenance of DSM programs. D.P.U. 95-30, at 29. The Department will review the DSM program designs and allocation of

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40 For example, customers on rate R-1 will experience rate reductions of approximately 12.1 to 12.2 percent over rates in effect as of August 1997 (Exh. EECo-1, Vol. 1, at 296).

funds in the Company's five-year energy efficiency plan filing to ensure an appropriate division of costs and expense recovery patterns among the various customer rate classes. Moreover, the Department intends to continue its monitoring of the Company's DSM programs targeted towards low-income customers to ensure that those programs provide genuine benefits to these customers.

E. Stranded Costs

1. Introduction

Stranded costs are fixed generating costs that would be "stranded" by the transition to competition, because they could not be recovered in the energy price for electricity in a competitive market. The Company estimated its stranded costs before mitigation at $601 million, which EECo states is $308 million less than the exit fee EECo would pay to Montaup under the FERC formula (Exhs. DPU-32; DPU-33). The Company proposes to collect its stranded costs in an access charge, which will be subject to annual reconciliation to actual costs and market conditions starting in 2001 (Exhs. EECo-1, Vol. 1, at 7-12). The Settlement provides that the Company mitigate, or reduce, its stranded costs by divesting, or selling, its generating assets, then flowing the benefits through to ratepayers via a residual value credit within three months after the assets are sold (id. at 21).

The Act adds to the Department's definition of stranded costs, expressed in D.P.U. 96-100, (1) employee-related transition costs such as severance pay and retraining for most employees, (2) property taxes or payments in lieu of property taxes, (3) removal and decommissioning costs for certain fossil-fueled generation, (4) post-shutdown nuclear costs besides decommissioning, and (5) buyout and buydown payments[41] for liquidating above-market PPAs. Section 193, Subsection 1G(b)(1).

[41] Such payments can also be viewed as mitigation of stranded costs, when taken together with the reduction in minimum payments under PPAs.

Parties did not contest the amount of EECo's potentially stranded costs. They did raise, however, the issues of whether the rate reduction resulting from divestiture will be as large as it should be and when it will be credited to customers. We will address these issues below.

2. Mitigation and Divestiture

a. Positions of the Parties

No party has contested the amount of EECo's stranded costs before mitigation. EECo notes that it has voluntarily committed itself to divest its generating assets in exchange for full recovery of fully mitigated stranded costs (EECo Brief at 10). EECo and the Attorney General add that the Settlement provides Montaup with meaningful incentives to mitigate stranded costs, which are designed to decline rapidly after three years (id. at 11; Attorney General Brief at 9). EECo maintains that the rapid decline in stranded costs supports the transition to competition (EECo Brief at 11). The Attorney General maintains that the Settlement's requirement that Montaup divest itself of non-nuclear plants not only eliminates affiliate transaction concerns, but will lower the concentration of ownership of generating capacity in New England and unbundle generation from transmission and distribution (Attorney General Brief at 6-7). DOER adds that divestiture will provide market valuation of Montaup's stranded assets (DOER Brief at 2).

b. Analysis and Findings

Section 193, Subsections 1A and 1G of the Act require that a company take all reasonable steps to mitigate its transition costs and, to that end, the Act encourages electric companies to divest their generating plants. Subsection 1G provides that a company that has a plan to divest its assets and mitigate its stranded costs may be entitled to recover its eligible transition costs.

The Department has reviewed the details of the Company's estimates of potentially stranded costs and finds that, subject to future market prices affecting PPA costs and nuclear decommissioning costs, the pre-mitigation amount of stranded costs claimed by the Company is accurate. The Department finds that the Company has committed to mitigation and divestiture of its generating plants, and therefore the Settlement is consistent with or in substantial compliance with the Act on this point.

Moreover, the Department finds that this Settlement provides for mitigation of stranded costs and contains appropriate incentives for the Company to maximize that mitigation, subject to its standard offer commitments. Mitigation by divestiture could significantly further reduce prices to EECo's customers. Divestiture, in addition to providing a true market valuation of stranded costs, may also reduce market power concerns related to affiliate transactions and concentrations of ownership. The Department finds that these are all very substantial benefits, which support five Department principles for restructuring: honoring existing commitments; providing near-term rate relief; ensuring an orderly and expeditious transition to competition; separating generation from transmission and distribution services; and employing incentive regulation.

3. Backstop Obligation and Increased Stranded Costs

a. Positions of the Parties

Several parties have raised the general concern, discussed above in connection with standard offer pricing, that Montaup's wholesale backstop obligation for standard offer pricing will act to increase stranded costs (XENERGY Brief at 14-20; Enron Brief at 11-13; Indicated Parties Brief at 7; NEV Brief at 3-5; Enron Legislative Comments at 2-8, citing Tr. 2, at 34-37, 42-43 and citing Exh. ECT-4 in D.P.U. 96-23). They argue that an obligation to supply wholesale power from the divested assets at the rates specified in the Settlement, when the power could actually be sold for a higher price in the wholesale market in the present or near future, diminishes the income that the new owner could expect from the divested assets (id.). Accordingly, they maintain, potential buyers for the assets will bid lower offer prices, in recognition of the lower income stream they would derive from the assets (id.). XENERGY estimates that the backstop provision will increase EECo's stranded costs by about $60 million[42] (XENERGY Brief at 17-18, citing Exh. Enron-11; RR-AG-1; Tr. 4, at 32, 188-189). Enron argues that this expected lower asset sale price associated with the backstop obligation would be inconsistent with the Act's requirements to (1) maximize the value of existing generation sold and (2) take all reasonable steps to mitigate transition costs (Enron Legislative Comments at 6, citing the Act, Section 193, Sections 1A(b)(1) and 1G(d)(1)).

In contrast, DOER, the Attorney General, and EECo argue that the backstop provision will not noticeably diminish the value of the assets sold (DOER Reply Brief at 3; Attorney General Reply Brief at 6; EECo Reply Brief at 7-8). DOER maintains that bidders will take many factors into account, and may view a backstop obligation as but a temporary hindrance (DOER Brief at 14). DOER allows that eliminating the backstop obligation, when market prices for electricity are high, may reduce stranded costs slightly, but argues that such an uncertain benefit will come at the cost of increasing risk of price volatility to customers, eliminating a certain benefit (id. at 13-14).

b. Analysis and Findings

Section 193, Section 1A(b)(1) of the Act requires, among other things, that an electric company divesting its generating units maximize their sale value. Section 1G(d)(1) requires that a company take all reasonable steps to mitigate to the maximum extent possible the total amount of transition costs recovered and to minimize the impact of such recovery on ratepayers.

The Department recognizes that some parties suggest that stranded costs would increase due to the backstop obligation. However, these parties have not demonstrated that wholesale electricity prices definitely will be above backstop prices nor that they would remain higher for long if they are. See the Department's discussion of XENERGY's analysis in Section VI.C.3,

42 See discussion in Section VI.C.2, above, for details of XENERGY's analysis.

above. Thus, any effect of the backstop provision on asset sales is speculative. Even if there were an increase in the value of the assets sold from eliminating the backstop obligation, that must be weighed against the increased risk of price volatility for customers.

More important, however, any increase in the sale price of divested assets due to eliminating the backstop obligation must be compared with the corresponding increase in the price of standard transition service.[43] Suppose the expected future income stream from the plants is the only factor in the bid price and that wholesale electricity prices exceed the backstop price for some time. If the backstop obligation were removed and the new owner of divested assets sold the output of plants in the open market, the income from the plants would be increased, by the quantity sold to standard offer customers times the difference between the eliminated backstop price and the actual market price. However, the surcharge to EECo's standard offer ratepayers (to recover the losses from retailing below the wholesale price) would increase by the difference between the eliminated backstop price and the actual market price. Consequently, the costs for standard offer customers[44] would increase by the quantity they buy times the difference between the eliminated backstop price and the actual market price. Thus, standard offer customers would pay the new owner of the plants the very income which led the new owner to pay more for the plants. Thus, Enron would have the Department take money

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[43] The actual price of assets sold, with or without a backstop obligation, results from many factors, including the different expectations of various bidders about future prices for the output of the generating units and perceptions of the value of the timing of resolving market uncertainties. In fact, some bidders may value only the plants' sites for the purpose of constructing new units there and thus would be indifferent to any projected income stream from the existing units. To further complicate the comparison between any higher sale price and higher standard offer charges, different interest rates apply to deferred standard offer charges and to charges for as-yet unrecovered stranded costs.

[44] To the extent the actual transition charge does not fall below the base case transition charges before 2004 and/or ratepayers leave the standard offer, the shortfall could be recovered from all ratepayers with interest starting in 2010, rather than just from standard offer customers.

from a ratepayer's transition charge pocket and move it to the ratepayer's standard offer service pocket.

Accordingly, the Department finds that removal of the backstop obligation is not likely to decrease ratepayers' overall costs, or to minimize the impact of transition cost recovery on ratepayers, but removal is likely to increase customers' risks and the price volatility they face. The Department does not view an action that is unlikely to appreciably reduce costs to ratepayers, but that does increase their risks and the price volatility they face, as a reasonable mitigation of stranded costs. Further, if a high bidder wants only the sites, removing the backstop obligation would not bring a higher price for the assets. Thus, whether removing the backstop obligation would maximize the sale value of generating units divested has not been convincingly established. Therefore, the Department finds that a backstop obligation does not interfere with taking all reasonable steps to mitigate transition costs to the maximum extent possible. Overall, the Department finds that the Company's mitigation plan based on divesting its non-nuclear generation, including the effect of the backstop obligation, substantially complies with the Act.

4. Mitigation Incentive and Amortizing the Residual Value Credit

a. Introduction

The Settlement provides Montaup with a monetary incentive to mitigate stranded costs and provides for amortization of the residual value credit ("RVC") over twelve years (Exh. EECo-1, Vol. 2, at 42-44, 46, 56-57).

b. Positions of the Parties

The mitigation incentive provides that all proceeds from divestiture, net of tax effects and any other adjustments approved by the Department that inure to the benefit of ratepayers, shall be applied to reduce the selling company's transition costs. Enron contends that this provision in the Settlement is inconsistent with the Act (id. at 9-10, citing Section 193, Subsection 1A(b)(3) of the Act). Enron also contends that amortizing the RVC over twelve years denies ratepayers a sizeable reduction in transition charges and thus is inconsistent with the Act (Enron Legislative Comments at 9).

EECo and the Attorney General argue that the Settlement provides Montaup with meaningful incentives to mitigate stranded costs, which are designed to decline rapidly after three years (id. at 11; Attorney General Brief at 9). EECo contends that not only is the transition charge consistent with the Act on its face, but the contract termination charge, including the mitigation incentive included in the Settlement, will, upon approval of the Settlement by FERC, be entitled to recovery under the filed rate doctrine (EECo Legislative Comments at 7, n.1).

c. Analysis and Findings

Section 193, Section 1G(b)(3) of the Act provides an incentive to reduce the transition charge, an incentive that is positive for transition charges below two cents per KWH and negative for transition charges above that level. This section also prohibits carrying costs on unamortized transition costs after 2009.

The Department notes that the mitigation incentive proposed in the Settlement is a very small proportion of the overall mitigation amount. The Department agrees with the Attorney General that it is a meaningful incentive to mitigate stranded costs as fully as possible, among other things by motivating the Company to (1) seek the highest price for its divested assets while minimizing its transaction costs in doing so and (2) renegotiate above-market PPAs more aggressively and creatively than command-type regulation could induce. Accordingly, the Department finds that the mitigation incentive inures to the benefit of ratepayers. Moreover, according to the filed rate doctrine, if FERC approves the Settlement including the mitigation incentive, the Department will be required to recognize in EECo's rates the amount Montaup collects from it for its mitigation incentive. Accordingly, the Department finds that the Settlement's mitigation incentive substantially complies or is consistent with the Act.

Regarding amortization, the Department notes that the present value of the RVC, amortized over any number of years, will be the same as long as the same discount rate is used. Amortizing the RVC over fewer years, as Enron advocates, could give ratepayers a bigger reduction earlier, followed by a rate increase. Such a rate increase would cause confusion and resentment among ratepayers, rather than benefitting them. Accordingly, the Department rejects Enron's contention that the Company's proposed amortization period is inconsistent with taking all reasonable steps to mitigate transition costs. The Department finds that the Settlement's proposed amortization period complies with the Act.

5. "Completion" of Divestiture

The Settlement states that upon "completion" of divestiture, ratepayers will receive a RVC against the access charge, and affiliates of Montaup will be free to re-enter the generation business (Exh. EECo-1, Vol. 1, at 37; Vol. 2, at 8, 31, 42).

a. Positions of the Parties

NEV is concerned that the divestiture and/or the resultant rate reductions will be delayed (NEV Brief at 17-19). First, NEV notes that divestiture does not have to happen by a specific time and advocates more stringent Department oversight of the timing to prevent delays (NEV Brief at 17). Second, NEV states that the Settlement suggests that divestiture will have to be completed before any RVC would be applied to the access charge (id.). NEV contends that divestiture of any substantial asset should trigger the RVC (id. at 18). Third, NEV contends that the RVC would not be applied to lower the access charge until 2001, via the reconciliation account (id.).

No party addressed NEV's concerns on brief. However, the Revisions provide that the RVC will apply within three months after the sale of any generating assets or other property subject to divestiture (Exh. EECo-2).

b. Analysis and Findings

Concerning NEV's first point, the timing of divestiture, the Department will continue its oversight of the Company's divestiture plans, through D.T.E. 97-105, the docket for the Company's divestiture plan filed on July 1, 1997.

Concerning NEV's second point, the Department finds that the Revisions satisfy NEV's and the Department's concern that the RVC should apply after the divestiture of any substantial asset. The Department finds that this revision will ensure that near-term rate relief will be provided in a timely manner, consistent with the Department's restructuring principles.

NEV's third concern is misplaced. The RVC affects the fixed portion of the access charge and applies within three months after asset sales. NEV is mistaken in its contention that the RVC acts through the reconciliation account, which NEV correctly observes would not lower the access charge until 2001.

Based on the foregoing, the Department finds that the Settlement's provisions on divestiture are consistent with or in substantial compliance with the Act.

F. Performance Standard Proposal

1. Introduction

The Settlement incorporates a performance standard component in EECo's proposed retail delivery rates, using outage duration and customer satisfaction indices as criteria (Exh. EECo-1, Vol. 2, at 198). The performance standard is intended to ensure that electric reliability and customer service standards are maintained during the term of the Settlement (Tr. 3, at 48). The Company states that the Settlement would not preclude the Department from investigating EECo's service quality if the Department deemed it appropriate (Tr. 3, at 55). Moreover, EECo states that it would have no objection to the adoption of additional criteria as part of an overall statewide performance standard, and indicates that it would have no objections to the consideration of additional performance criteria in a future Company-specific proceeding, such as a base rate proceeding (Tr. 3, at 54-55). Also, as noted above, the Company filed a proposal for line loss performance standards on October 1, 1997.

2. Positions of the Parties

a. LII

The LII maintain that the Settlement is inconsistent with the Act, because the service quality standards provided for under the Settlement would allow for substantial declines in quality of service (LII Legislative Comments at 5). The LII contend that while the outage duration index is a reasonable standard in concept, the latitude of service performance deterioration allowed the Company before penalties take effect renders the standard meaningless (LII Brief at 2). The LII note that the proposed standard's reliance on aggregated circuits allows poorly-performing circuits to be masked by better-than-average performing ones, and that the standard fails to account for other service quality indicators for which EECo maintains data, such as safety and power quality (id., citing Exhs. LII-5, LII-6, LII-11, at 3).

b. Attorney General

The Attorney General argues that the performance standards included in the Settlement are intended only to provide assurance against service degradation during the three-year price freeze under the Settlement (Attorney General Brief at 21-22). Moreover, the Attorney General maintains that the Settlement's performance standards are expressly subject to being superseded by more stringent performance standards that may be later adopted by the Department through a generic proceeding (id. at 22; Attorney General Reply Brief at 3).

c. The Company

The Company argues that the performance standards under the Settlement are consistent with the Act, because the Settlement does not preclude the Department from promulgating additional standards that would be required by the Act (Company Legislative Comments at 9). EECo identifies the Settlement's performance standards as protecting customers from service quality deterioration, not as a comprehensive set of standards (id.).

The Company contends that the LII's criticisms of the Settlement's performance standards should carry no weight (Company Reply Brief at 23). EECo reasons that because the National Consumer Law Center, which the Company presumes shares the interests of the LII,[45] was a signatory to the settlement in D.P.U. 96-25 which contained virtually identical provisions, these terms of the Settlement are reasonable and in the public interest (id. at 23-24).

3. Analysis and Findings

Section 193, Subsection 1E of the Act authorizes the Department to promulgate rules and regulations to establish performance-based rates for distribution companies, including a number of standards which are specified under the Act. The Act also permits the Department to penalize a distribution company which fails to meet the service quality standards adopted under this provision in an amount up to 2.0 percent of such company's transmission and distribution service revenue for the previous calendar year.

While the performance standards proposed in the Settlement are less comprehensive than those which the Act requires the Department to incorporate into performance-based rate mechanism, the Department finds that the performance-based regulation features of the Settlement are not intended to serve as a broad-based incentive regulation framework, but to provide ratepayers with a level of protection against a decline in service standards by ensuring historic levels of reliability and customer service. In addition, we note that the Company has agreed to comply with additional performance-based rate standards promulgated by the Department on either a generic or company-specific basis pursuant to the Act. Accordingly, the Department finds that the performance standards provided as part of the Settlement are consistent with or in substantial compliance with the Act.

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45 EECo asserts that the National Consumer Law Center appears to be representing the interests of the LII, as well as two of the signatories to the Settlement (id. at 23-24).

Concerning the LII's concerns about the effectiveness of the Settlement's performance standards, the Department notes that the nature of settlements provides for compromise between the varying interests of negotiating parties.[46] While the performance standards proposed here are less comprehensive than those adopted in Boston Gas Company, D.P.U. 96-50 (1996), and NYNEX, D.P.U. 94-50 (1995), we approve the Settlement upon the premise that its terms do not preclude the adoption of additional or more stringent criteria in either a Company-specific or industry-wide proceeding. We take the Company's acceptance of this Order as its agreement with this construction. Consistent with Incentive Regulation, D.P.U. 94-158 (1995) and the Act, the Department expects the Company to address performance-based regulation issues after the conclusion of the rate freeze period. See also Electric Restructuring, D.P.U. 96-100, at 116 (1996).

Concerning the Company's proposed line loss standard, the Department notes that this performance standard had not been developed and submitted until after the close of hearings. Accordingly, the Department finds that it would be premature at this time to rule on the merits of the proposed line loss standard. The Department shall address this issue separately in the future.

G. Other Issues

1. Emission Reductions

a. Introduction

The Settlement requires emission reductions from Montaup's major generating units, Somerset and Canal, and specifies that nothing in the Settlement shall affect Montaup's obligations to comply with lawful regulations imposing new environmental standards (id., Vol. 1, at 25, Vol. 2, at 240-242).

[46] Neither the National Consumer Law Center nor any of the other entities that compose the Low-Income Intervenors signed the settlement which is the subject of this proceeding.

b. Positions of the Parties

No party has contested the Settlement's provisions for emission reductions. EECo states that the emission reductions provisions are very similar to those approved in D.P.U. 96-25 (EECo Brief at 6-7). The Attorney General and the DOER maintain that the voluntary emission reductions provisions in the Settlement implement the Department goal of reducing the environmental impacts of electricity generation in a cost-effective manner, consistent with the statutory requirement to maintain safe and reliable electric service with minimum impact on the environment (Attorney General Brief at 8-9; DOER Brief at 2, 4).

c. Analysis and Finding

Section 105 of the Act requires the Department of Environmental Protection to promulgate rules and regulations establishing uniform generation portfolio emission standards for fossil fuel-fired generating plants. The Settlement specifies that nothing in the Settlement shall affect Montaup's obligations to comply with lawful regulations imposing new environmental standards. Accordingly, the Department finds that the Settlement complies with the Act in this regard. Further, the Department finds that the emissions provisions of the Settlement reduce the environmental impacts of electricity generation, consistent with our mandate to provide power with minimum impact on the environment at the lowest possible cost and with our principle of supporting the goals of environmental regulation.

2. DSM

a. The Act

Section 37 of the Act requires a charge to fund cost-effective DSM programs for at least five years, consisting of 3.3 mills ($0.0033), 3.1 mills, 2.9 mills, 2.7 mills, and 2.5 mills per KWH for the years 1998 through 2002, respectively. At least 20 percent of the residential portion, and at least 0.25 mills per KWH, must be used for low-income DSM and education programs. Section 50 of the Act authorizes the DOER to oversee and coordinate ratepayer-funded DSM, with goals including equity among customer classes, low-income and weatherization programs, and support for lost opportunity programs, including statewide market transformation efforts. The DOER will file an annual report with proposed DSM funding levels to implement programs for the Department's approval where it finds the programs cost-effective.

b. The Settlement

The Settlement requires EECo to submit to the Department budgets for DSM, including market transformation, based on a charge of 3.0 mills per KWH during 1998, 1999, and 2000, followed by a charge of 2.75 mills in 2001 (Exh. EECo-1, Vol. 1, at 26-27). At least 15 percent of the DSM budget must be spent on residential programs, with at least 15 percent of that for low-income programs, including specific amounts for weatherization and fuel assistance (id.).

c. Positions of the Parties

CLF contends that "substantial compliance" with the Act requires the DSM funding levels and implementation of the DSM policies specified in the Act (CLF Legislative Comments at 2). The Company contends that while the Settlement's numbers do not match exactly the Act's numbers, the commitment to these programs substantially complies with the Act (EECo Legislative Comments at 11).

Enron opposes EECo's planned expenditure of up to $0.8 million in ratepayer funds for sophisticated metering and control technology, to be used to target DSM that could reduce distribution line losses, claiming that this could stifle competition in metering, billing, and information services ("MBIS") (Enron Brief at 24-25, citing Tr. 2, at 45-47). Enron plans to pursue this issue in the investigation into EECo's five-year energy efficiency plan filing (Enron Brief at 26).

No party has contested the Settlement's other DSM provisions. The Attorney General points out that the Settlement increases DSM funding by a third from current levels, and specifically targets low-income customers (Attorney General Brief at 12). The Attorney

General adds that continued DSM funding helps reduce the environmental impacts of electricity generation, a Department goal (Attorney General Brief at 8). DOER claims that EECo's proposed DSM funding levels will provide valuable services to customers and are consistent with those approved for MECo (DOER Brief at 9, citing Exh. DPU-4). DOER observes that specific DSM program plans are subject to Department approval in a separate docket (DOER Brief at 9, citing Exh. DPU-4).

d. Analysis and Findings

The Settlement requires the Company to file a DSM budget and the Act requires the DOER to file a budget, both for the Department's approval. The Department will have two versions of the Company's DSM budget to review. Moreover, the Act prescribes the income for DSM programs; while a budget targets the expense. DSM income generally differs from DSM expenditures; therefore, the Department has provided for retrospective reconciliation of DSM income to DSM expenditures and will continue to do so. Therefore, the Department finds that the Settlement's overall DSM budget provision substantially complies with the intent of the Act.

The Act requires that 20 percent of DSM funds be spent on residential programs generally and low-income programs specifically, while the Settlement requires that at least 15 percent is spent on these programs. We note that nothing in the Settlement prevents the Company from spending 20 percent on such programs. Therefore, the Department finds that this provision of the Settlement substantially complies or is consistent with the Act.

The Department finds that the Settlement's DSM provisions provide substantial benefits, including reducing the environmental impacts of electricity generation, consistent with the Department's statutory mandate and with the Department's goals of maintaining DSM programs and furthering the goals of environmental regulation. See D.P.U. 95-30, at 16-17, 30, 44-45. Accordingly, the Department finds that this feature of the Settlement is in the public interest. The Department will review program plans, budgets, and the relation of DSM to MBIS in the investigation into EECo's five-year energy efficiency plan, docketed as D.P.U. 97-91.

3. Renewables

a. The Act

Section 37 of the Act requires a charge to fund renewable energy projects, with the fund to be administered by the Massachusetts Technology Park Corporation ("MTPC"). The charge, to maximize economic and environmental benefits over time from renewable energy for Massachusetts, starts at 0.75 mills per KWH in 1998, followed by 1.00, 1.25, 1.00, and 0.75 mills in each of the years 1999 to 2002, then 0.50 mills per KWH thereafter. Section 68 of the Act defines renewable energy eligible for funding from the ratepayer charge to include solar, wind, ocean-derived energy, landfill gas, advanced biomass, most fuel cells, MSW, hydro, and storage and conversion technologies connected to qualifying projects.

b. The Settlement

The Settlement requires EECo to submit renewable energy budgets to the Department for 1998, 1999, 2000, and 2001 based on charges of 0.25, 0.55, 0.85, and 1.25 mills per KWH, respectively (Exh. EECo-1, Vol. 1, at 27). The Settlement defines eligible renewable energy sources as those specified in Section 68 of the Act, but without MSW, hydro, or storage and conversion technologies (id. at 28-29).

c. Positions of the Parties

CLF contends that "substantial compliance" with the Act requires the renewables funding levels and implementation of the renewables policies specified in the Act (CLF Legislative Comments at 2). EECo contends that while the Settlement's numbers do not match exactly the Act's numbers, the commitment to these programs substantially complies with the Act (EECo Legislative Comments at 11). The Attorney General adds that funding for renewables helps reduce the environmental impacts of electricity generation, which is a Department goal (Attorney General Brief at 8).

d. Analysis and Findings

The Department notes that, under the Settlement, the Company proposes to implement renewables charges over the period 1998-2001. While the renewables charges proposed by the Company are, for the early years, lower than the renewables charges stated by the Act, the Department notes that the Company intends to augment its renewables activities with existing funds. Specifically, the Department notes that, under the Settlement, the Company proposes to retain $4.18 million of DSM overrecovery for the express purpose of mitigating phased-in increases to its DSM and renewables budgets over the period 1998-2001, and to prefund the renewables amount as of January 1, 1998. Accordingly, based on the Company's renewables charges and its use of existing funds for renewable energy purposes, the Department finds that the Company's renewables proposal substantially complies with or is consistent with the Act.

Moreover, the Department finds that the Settlement's renewables provisions provide substantial benefits, including reducing the environmental impacts of electricity generation, consistent with the Department's statutory mandate and furthering the goals of environmental regulation. See D.P.U. 95-30, at 16-17, 30, 44-45. Accordingly, the Department finds that this feature of the Settlement is in the public interest.

4. Low-Income, Safety Net and Basic Service

a. Introduction

The Settlement provides for low-income discounts for eligible customers, safety net service for customers unable to obtain or retain electric service from competitive power suppliers, and basic service for customers who may be temporarily without a contractual relationship with a power supplier (Exh. EECo-1, Vol. 1, at 22, 30).

b. Positions of the Parties

(1) LII

The LII contend that the Settlement fails to comply with the Act, pointing out that while the Act specifies that any customer receiving any means-tested public benefit, or who is eligible for the Low Income Home Energy Assistance Program ("LIHEAP"), receive discounted rates, the Settlement provides discounted rates only for customers receiving certain enumerated public benefits (LII Legislative Comments at 4-5). The LII point out that the Act allows low-income customers to return to the standard transition service rate at any time (id. at 4). The LII add that the Settlement fails to provide a comprehensive outreach plan to notify and provide eligible customers discounted rates, as required by the Act, although the record demonstrates that the Company is already doing some outreach (id. at 5).

The LII fault the "safety net service" and "basic default service" features of the Settlement (LII Brief at 2). According to the LII, while "safety net service" is a good concept, the lack of definitions for such service, such as what constitutes a "low-income" customer and under what conditions a customer is considered unable to obtain market supply, renders "safety net service" open to continued questions (id.). The LII contend that procuring supplies for default service from the spot market, as provided in the Settlement, is inconsistent with the Act's requirement that the price of default service not exceed the average monthly market price for electricity (LII Legislative Comments at 4).

(2) Attorney General

The Attorney General maintains that the Settlement is in substantial compliance with the Act (Attorney General Legislative Comments at 1). The Attorney General contends that the conditions requested by the LII concerning service to low-income customers, such as safety net service, do not have to be resolved in this proceeding and are more properly the subject of other dockets (Attorney General Reply Brief at 2-3).

(3) The Company

The Company argues that the Settlement provides for basic and default service, in compliance with the Act (Company Legislative Comments at 6). EECo maintains that the Act requires utilities to provide discounted rates for low-income customers which are comparable to those currently in effect, which the Company argues is specifically provided for under the Settlement (id. at 10).

The Company contends that the LII's criticisms of the Settlement's basic and safety net services should carry no weight (Company Reply Brief at 23). EECo reasons that because the National Consumer Law Center, which the Company presumes shares the interests of the LII, was a signatory to the settlement in D.P.U. 96-25 which contained virtually identical provisions, these terms of the Settlement are reasonable and in the public interest (id. at 23-24).

c. Analysis and Findings

Section 193, Subsection 1F(4) of the Act requires that electric companies provide discounted rates for low-income customers, with guaranteed payments to suppliers, comparable to those in effect as of March 1, 1998, to customers who receive any means-tested public benefit or are eligible for the LIHEAP. An electric company must use outreach efforts to provide the low-income discount rate to eligible customers. The standard service transition rate must be available at any time to customers eligible for low-income programs. Subsection 1B(d) requires distribution companies to provide default service for customers who are unable to obtain electric service from competitive power suppliers, by reason of a failure of the supplier or distribution company, the expiration of the customer's standard offer term, or through the customer's inability to obtain standard offer service. This Subsection requires default service to be procured by competitive bidding, provided that the rate not exceed the average monthly market electricity price, with payment options including uniform rates for up to six months. Subsection 1B(f) authorizes the Department to promulgate rules and regulations necessary to carry out this provision, including the procedure for default service procurement.

The Settlement provides for both safety net and basic service. The Settlement is silent on the specific terms and conditions under which a customer would be eligible for safety net service or default service. Therefore, our acceptance of the Settlement would not preclude further examination of these issues as they arise. The Department finds that most of these and related issues are best addressed in D.P.U. 97-65, or in a separate proceeding.[47] However, as the LII point out, the Company must procure supplies for default service from the short-term wholesale market by competitive auction with the constraints specified in the Act. The Department finds that the Settlement substantially complies with the Act on this point; the Company will simply need to take further steps within the framework of the Settlement to comply with the section of the Act referenced by the LII. Accordingly, the Department finds that, overall, the Settlement's provisions on basic and default service are consistent with the Act.

Turning to the Company's low-income rates, the Department finds that the Settlement provides for discounted low-income rates which are comparable to EECo's current low-income rate R-2. The Department intends to address the expansion of eligibility requirements as part of promulgating our final rules in D.P.U. 96-100. Accordingly, the Department finds that the Settlement substantially complies or is consistent with the Act.

5. Storm Fund

a. Introduction

As described above, the Settlement permits EECo to create a storm reserve fund to cover the expense associated with storms that result in incremental costs exceeding $250,000 (Exh. EECo-1, Vol. 1, at 13). The Company will prefund the storm reserve by transferring a sum of up to $2 million from the Montaup 1996 PCAC refund to the Company, and as of the retail access date, the Company's retail rates will be deemed to provide for a $1.3 million annual accrual to the storm reserve fund (id.).

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47 The Department notes, again, that neither the National Consumer Law Center nor any of the other entities that comprise the Low-Income Intervenors signed the Settlement which is the subject of this proceeding.

b. Positions of the Parties

The LII criticize the Settlement's inclusion of a storm fund, stating that the Company's current rates already incorporate expenses from two major storms (LII Brief at 1, citing Exh. LII-9; RR-LII-2). No other parties commented on this issue.

c. Analysis and Findings

The Act is silent on the issue of creating storm funds. Nevertheless, the Department finds that the Settlement's provisions concerning the storm fund are consistent with or substantially comply with the Act and do not frustrate the Act's intent.

With respect to the Settlement's provisions on the storm fund, the proposed standard offer retail delivery rates which include provision for a storm fund will remain in effect at least through December 31, 2000, after which the Settlement is silent on the storm fund's continuation. The creation of a storm fund was the result of a balancing of interests among various parties. Therefore, our acceptance of the Settlement here does not bind the Department to perpetuate the existence of a storm fund in future rate or any other proceedings. See Dover Water Company, D.P.U. 90-86, at 4-5 (1990). Accordingly, considering a balancing of interests among the various parties, the Department finds that this provision is in the public interest.

6. Employee Issues

a. Introduction

The Settlement provides that all reasonable costs and expenses incurred by Montaup or its affiliates associated with the implementation of retail access, divestiture, or termination of Montaup's tariff, such as early retirement, severance, retraining, and other related expense, shall be incorporated in the access charge (Exh. EECo-1, Vol. 2, at 51-52).

b. Positions of the Parties

(1) MAUU

The MAUU contends that, because a shift to incentive regulation must not be at the expense of service quality, the Department must undertake a pre-incentive regulation review of historical staffing levels and employee training program levels for all electric utilities to develop appropriate benchmarks (MAUU Brief at 2). The MAUU also argues that "stranded human investment" is just as important as "stranded investment" (id. at 2-3). Therefore, the MAUU proposes that any sale of facilities resulting from the Settlement should be conditioned on (1) retaining the workforce for at least three years, or in the alternative, the Company contracting with the new owner to be responsible for operation and maintenance of plant; (2) new owners being required to recognize the existing union as the collective bargaining agent; and (3) providing sufficient severance packages for those employees who are not retained by the new management (id. at 4).

(2) Attorney General

The Attorney General notes that the Settlement already provides for the flow-through of costs relative to employee severance and retraining (Attorney General Reply Brief at 2). In addition, the Attorney General argues that any concerns over continued service quality are capable of being resolved through a generic proceeding (id. at 3).

(3) The Company

The Company argues that MAUU failed to support its arguments on the record (Company Reply Brief at 23). The Company maintains that the employee issues cited by MAUU have been provided for through the Settlement's provisions on recovery of severance and retraining expenses through the access charge (id. at 22). EECo argues that the specific values of these various packages are best left to be worked out between the Company and MAUU, instead of being mandated by the Department (id. at 23). Referring to the

Department's disposition of these identical issues in D.P.U. 96-25, EECo concludes that the MAUU's concerns do not detract from the reasonableness of the Settlement (id.).

c. Analysis and Findings

Section 193, Subsection 1E of the Act prohibits any electric distribution or transmission company filing a performance-based regulation proposal after the effective date of the Act; i.e., November 25, 1997, from engaging in labor displacement or staffing reductions below those levels in effect on November 1, 1997, unless such reductions are the result of collective bargaining, Department approval after evidentiary hearings, or early retirement and severance packages entered into before November 1, 1997. The presence of provisions governing the recovery of severance and retraining packages through access charges presupposes that such packages may eventually be developed, and we expect that the Company will comply fully with the Act while it negotiates with its union workforce, through their respective bargaining units, on such packages. Accordingly, the Department finds that the Settlement's provisions on employee issues are consistent with or in substantial compliance with the Act.

With respect to the MAUU's concern that the Settlement will result in employee layoffs and thereby a degradation of service quality or system reliability, the Department notes that one of our explicit goals in restructuring is to maintain safe and reliable service. Our restructuring plan in D.P.U. 96-100 addresses a number of specific mechanisms to achieve this, both in the unregulated generation market and in the regulated transmission and distribution operations. These include competitive supplier requirements and consumer protection regulations. Further, the Department will continue to oversee all distribution companies. Any action by a distribution company that compromises safety or reliability is unacceptable, and the Department will exercise its authority to ensure a high level of reliability. D.P.U. 95-30, at 1-2; Electric Restructuring Plan: Model Rules and Legislative Proposal, D.P.U. 96-100, at 32-33, 46-51 (1996). See also Incentive Ratemaking, D.P.U. 94-158, at 59-60 (1995). There are no provisions in the Settlement that limit the ability of the Department to require EECo and other utilities to maintain and improve current standards of service quality and system reliability. There is every reason to expect that the Company and Montaup will work in a cooperative manner with their union workforces, through their respective bargaining units, to resolve any outstanding issues among themselves. Therefore, the Department finds that acceptance of the Settlement does not compromise employee and safety issues.

7. Proposed Unbundled and Retail Access Tariffs

a. Introduction

As part of the Settlement, EECo has submitted two sets of tariffs: the first set consists of unbundled tariffs M.D.P.U. Nos. 322 through 337, that would remain in effect until the retail access date, i.e., March 1, 1998; the second set consists of the Company's retail delivery tariffs M.D.P.U. Nos. 338 through 356, which incorporate the standard offer option that will take effect as of the retail access date (Exh. EECo-1, Vol. 1, at 7).

b. Positions of the Parties

(1) New Energy Ventures

NEV contends that the wording of the ACAC implies that the access charge will remain at 3.04 cents per KWH until January 1, 2001, even if significant mitigation occurs from the sale of Montaup's generating assets (NEV Brief at 19). NEV urges the Department to make it clear that the access charge can and will fall below 3.04 cents per KWH prior to January 1, 2001 (id.).

(2) The Company

The Company notes that the unbundled rates provided for under the Settlement are consistent with the Act, because charges on customers' bills have already been unbundled to separately identify generation, transmission, and distribution (Company Legislative Comments at 6-7).

During the hearings, the Company conceded that the wording of the proposed ACAC tariff, M.D.P.U. No. 339, was misleading, and offered the following amended language (Tr. 3, at 43-44).

> The initial termination charge included in overall base rates shall be [3.04 cents]/KWH through December 31, 2000. Thereafter, an Access Cost Adjustment Factor shall be computed to reflect the difference between the initial termination charge and the actual termination charge each time that the termination charge that MEC [Montaup] bills to the Company changes. The Access Cost Adjustment Factor shall be applied on an equal cents-per-KWH basis to all Company rate classes (Exh. DPU-26).

Subsequently, EECo submitted as part of the Revisions to the Settlement a new ACAC tariff reflecting the language contained in Exhibit DPU-26, with additional language to indicate that the residual value credit would be that allowed by the FERC, upon the divestiture of Montaup's non-nuclear generating units as it occurs (Exh. EECo-2).

c. <u>Analysis and Findings</u>

Section 193, Subsection 1D of the Act requires that a customer's electric bill show separate rates for distribution, transmission, and generation charges by January 1, 1998, with any transition charges to be reflected separately by March 1, 1998. The Act permits customers to receive either a single bill from the distribution company, or to be billed separately for generation and distribution services. Because the Company has already unbundled its bills, the Department finds that the Settlement is consistent with the Act.

With respect to the unbundled tariffs, M.D.P.U. Nos. 322 through 337, the Department directs the Company to resubmit these tariffs replacing the effective date of July 1, 1997 with an effective date consistent with the date of this Order. With respect to the retail delivery tariffs, M.D.P.U. Nos. 338 through 356, the Department accepts these as filed, subject to the conditions described below for M.D.P.U. No. 339, Access Cost Adjustment Clause, and M.D.P.U. No. 340, Standard Offer Service, as well as the amendments necessary to provide for the additional 10 percent discount offered to agricultural customers pursuant to Section 315 of the Act. The Department directs the Company to resubmit M.D.P.U. Nos. 338 through 356 incorporating these modifications, with an effective date of March 1, 1998.

The Department has examined the Company's revisions to proposed tariff M.D.P.U. 339 as found in Exhibit EECo-2, and finds that the revised language accurately reflects the conditions under which the ACAC would be developed and applied. Boston Gas Company, D.P.U. 92-259, at 47 (1993); Dedham Water Company, D.P.U. 13271, at 10 (1961). See also G.L. c. 164, § 94; 220 C.M.R. §§ 5.00 et seq.. Moreover, the Department finds that the revised tariff language addresses the concerns of NEV. Accordingly, the Department accepts the Company's revised tariff M.D.P.U. No. 339.

The Department has also examined the Company's revisions to proposed tariff M.D.P.U. No. 340 as found in Exhibit EECo-2, and finds that the revised language accurately reflects the fact that standard offer customers may elect to continue taking standard offer service if they relocate within the Company's service territory. However, the Act provides that low-income customers may switch at any time from competitive service to standard offer service. Accordingly, the Department hereby directs the Company to revise M.D.P.U. No. 340 to specify that low-income customers may switch between competitive service and standard offer service. The Department will address the expanded eligibility requirements for low-income rates as part of its final rules in D.P.U. 96-100.

H. Conclusion

As stated in our standard of review, above, the primary goal of the Act is to establish a new electric utility framework under which competitive producers will supply electric power and customers will gain the right to choose their electric power supplier in order to promote reduced electricity rates. The Act requires that all restructuring plans must contain two key features. Each plan must provide, by March 1, 1998, for a restructured electric generation market that offers retail access to all customers and for a rate reduction of 10 percent for customers choosing the standard service transition rate. In addition, each plan should include an estimate and detailed accounting of transition costs, a description of a company's strategy to mitigate transition costs, unbundled prices for generation, distribution, transmission, and other services, charges for transition cost recovery, programs to provide universal service, programs for energy conservation and demand-side management, procedures for ensuring direct retail access to all electric generation suppliers, and discussions of the impact of the plan on the Company's employees and the communities served by the Company.

The Act states that an electric company that has filed a plan which substantially complies or is consistent with this chapter as determined by the Department shall not be required to file a new plan, and the Department shall allow such plans previously approved or pending before the Department to be implemented. In determining whether the Company's plan substantially complies or is consistent with the Act and meets the requirements of any other applicable law, the Department has considered the stated purposes and major features of the Act as a whole and determined that the plan substantially complies or is consistent with the Act as a whole. As it must under the terms of the Act, the Department approves the Company's plan.

In setting the standard of review, the Legislature recognized that one settlement had already been approved and that there were settlements pending before the Department.[48] Therefore, in order to retain the value of extensive negotiated settlements among a divergent group of signatories, the Legislature did not require strict compliance with every provision of the Act; instead it stated that these settlements must be evaluated based upon consistency with or substantial compliance with the Act, not precise compliance with every detail. To be approved as in substantial compliance, a settlement need not comply strictly point by point with the Act, but must, on the whole, satisfy the Act's stated goals and main features.

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[48] At the time of enactment, the Department had approved a settlement for Massachusetts Electric Company. In addition, EECo and Boston Edison Company had filed settlements upon which an extensive record had been developed.

Further, the Legislature evidenced its intention that the Department move with dispatch to review the settlements already filed by declaring the Act to be an emergency law. The preamble states that:

> …the deferred operation of this act would tend to defeat its purpose, which is to establish forthwith a comprehensive framework for the restructuring of the electric utility industry, to establish consumer electricity rate savings by March 1, 1998, and to make certain other changes in law….

The Legislature clearly expected the Department to move swiftly to provide for direct retail access and a 10 percent rate reduction by March 1, 1998. Therefore, we must consider the Settlement and make a determination whether it satisfies, on the whole, the stated goal and main features of the Act.

Clearly, the Settlement substantially complies or is consistent with the stated goal and main features and achieves actual compliance with the essential requirements of the Act: provision of customer choice of generation supplier by March 1, 1998; a 10 percent rate reduction for customers choosing the standard offer; an accounting of stranded costs and a mitigation plan based on the sale of the generating plant; a non-bypassable charge to collect stranded costs; the provision of standard offer service for seven years; unbundled rates; a general inflation cap and a cap on the stranded cost charge; default service; a provision for the funding of renewable energy; and continuation of low-income discounts, universal service, and DSM. Further, the Settlement does not prevent the Company from complying with regulations implementing performance standards and rules of conduct regarding affiliates. In addition, the Department finds that the Settlement is consistent with the provision for payments in lieu of property taxes and for generating performance standards. Finally, the Settlement substantially complies with the DSM and Renewable Energy provisions of the Act. Therefore, the Department finds that the Settlement, as a whole, substantially complies or is consistent with the Act.

Since the Settlement is consistent with the Act and will accomplish the purposes of the Act, the Department hereby approves the Settlement, will not require the Company to file a new plan and will allow the plan in the Settlement to be implemented. Further, since the Company has met the conditions specified in the Act, the Department hereby authorizes the Company to collect a transition cost charge as specified in the Act, provisionally[49] according to the formulas embodied in the Settlement, upon its commencement of actual mitigation efforts and the implementation of retail access.

As stated in our standard of review for settlements, the Department must review the entire record to ensure that the Settlement is consistent with applicable law, including relevant provisions of the Act, Department precedent and the public interest. To determine whether the Settlement is consistent with Department precedent, the Department will consider whether the Settlement is consistent with the overall goal and principles for restructuring that were established in D.P.U. 95-30, and affirmed in D.P.U. 96-100. The Department must conclude that the Settlement will result in a just and reasonable outcome.

We have separately analyzed the Settlement on the following issues to determine if it meets our standard of review for approval of a settlement: standard offer; stranded costs; performance standard proposal; emission reductions and renewables; demand-side management; safety net and basic service; storm fund; employee issues; and proposed unbundled and retail access tariffs. We have made subsidiary findings regarding the merits of the Settlement on these issues and their consistency with our restructuring principles.

Just as the Settlement represents a compromise among the various signing parties and is presented to the Department on the condition that it be approved in full, the Department's

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[49] The Company must revise the formulas, when the residual value credit is applied, to reflect the Act's provisions regarding the return on equity for as-yet unrecovered transition costs, and may need to revise the formulas to comply with the Act if (1) the sum of proposed transition costs not allowed by the Act exceeds zero or (2) the residual value credit alone is insufficient to bring the total rate reduction to 15 percent by September 1, 1999.

ultimate conclusion must be one based upon the entirety of the Settlement and not solely on an issue by issue critique. Even if the Department determined that the Settlement's resolution of certain issues was less than optimal, we could approve the Settlement as being on the whole just and reasonable, consistent with Department precedent, and in the public interest.

In conclusion, the Department finds that the provisions of the Settlement Agreement and the Revisions, that are within the scope of this proceeding, in their entirety, are consistent with (1) the Act; (2) our primary objective to reduce costs, over time, for all consumers of electricity; (3) our goal to develop an efficient industry structure and regulatory framework that minimize costs to consumers while maintaining safe and reliable electric service with minimum impact on the environment; and (4) the Department's electric industry restructuring principles and proposal. Therefore, the Department finds that the provisions of the Settlement Agreement and the Revisions, that are within the scope of this proceeding, represent, on balance, a just and reasonable resolution of restructuring issues for the Company and its ratepayers, and thus, are in the public interest.[50] Accordingly, pursuant to our authority to regulate the operations of the electric utility companies in Massachusetts under G.L. c. 164, §§ 76 and 94,[51] the Department approves the following provisions of the Settlement Agreement and the Revisions:

§ I. Price Reductions for All Customers, including (A) a 10 percent price reduction for EECo's customers, including recovery of stranded costs in a retail access charge, (B) a

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50 Failure by the FERC to approve the wholesale rate stipulation and agreement would render the Settlement Agreement null and void, and of no effect. Approval of the Settlement, unless otherwise agreed to by the Department, is limited to the wholesale rate stipulation and agreement, as filed. FERC approval of provisions to the wholesale rate stipulation and agreement other than as filed with the Department must be submitted for Department review.

51 See also D.P.U. 96-100 (December 30, 1996) at 22-23 n.16, n.17, 231-234, 264-268; D.P.U. 95-30, at 33-34, 40-44.

distribution rate freeze, and (C) EECo's right to file for a rate change in the event that the retail access date has not occurred by January 1, 2001;

§ II. Benefits of Competition Extended to All Customers, including (A) the opportunity to choose alternative suppliers and a guarantee of significant rate reductions for customers who choose the standard offer and (B) the implementation of retail access;

§ III. Protect the Environment and Promote Conservation, including (A) emissions reductions and (B) increased funding for DSM and renewables;

§ IV. Protect Low-Income Customers, including the continuance of the low-income customer discount, protection against redlining, and the continuance of programs and mechanisms that enable residential customers with low incomes to manage and afford electricity requirements;[52]

§ VI. Successors and Assigns, including the rights and obligations imposed on any signatory to the Settlement; and

§ VII. Additional Provisions, concerning the protection of settlement negotiations and the precedential effect of the Settlement.

The Department notes that our acceptance of the Settlement and Revisions does not result in a finding on the merits of any issue outside the context of the Settlement and Revisions and does not set a precedent for future restructuring filings, whether ultimately adjudicated or settled.

52 The Department does not act, at this time, on the provisions of § V that include (A) Regional Reform, (B) the jurisdictional separation between transmission and distribution (See D.P.U. 97-93), and (E) customer service standards (See D.P.U. 97-65). These are not conditions of the Settlement and Revisions.

VII. ORDER

Accordingly, after due notice, hearing, and consideration, it is

ORDERED: That the tariffs of Eastern Edison Company for bundled generation and distribution service, M.D.P.U. Nos. 322 through 337, which would apply to electric service consumed on or after July 1, 1997, be and hereby are DISALLOWED; and it is

FURTHER ORDERED: That Eastern Edison Company shall file tariffs for bundled generation and distribution service, also to be designated as M.D.P.U. Nos. 322 through 337, which shall be consistent with the directives of this Order and shall apply to electric service consumed on or after the date of this Order; and it is

FURTHER ORDERED: That the tariffs of Eastern Edison Company for retail delivery service, M.D.P.U. Nos. 338, 339 as revised, 340 as revised, and 341 through 356, which shall apply to electric service consumed on or after the retail access date, be and hereby are DISALLOWED; and it is

FURTHER ORDERED: That Eastern Edison Company shall file tariffs for retail delivery service, also to be designated as M.D.P.U. Nos. 338 through 356, which shall be consistent with the directives of this Order and shall apply to electric service consumed on or after March 1, 1998; and it is

FURTHER ORDERED: That the provisions of the Settlement and Revisions listed as conditions in the Settlement and Revisions be and hereby are APPROVED; and it is

FURTHER ORDERED: That Eastern Edison Company shall comply with all orders and directives contained herein.

By Order of the Department,

Janet Gail Besser, Acting Chair

John D. Patrone, Commissioner

James Connelly, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).